S. HRG. 107–1068

“PROMISES MADE, PROMISES KEPT: ARE INTERNATIONAL TRADE AGREEMENTS REALLY INVESTMENT AGREEMENTS?”

HEARING

BEFORE THE

COMMITTEE ON COMMERCE, SCIENCE, AND TRANSPORTATION UNITED STATES SENATE

ONE HUNDRED SEVENTH CONGRESS

FIRST SESSION

AUGUST 1, 2001

Printed for the use of the Committee on Commerce, Science, and Transportation

U.S. GOVERNMENT PRINTING OFFICE

89–446 PDF WASHINGTON : 2004

For sale by the Superintendent of Documents, U.S. Government Printing Office
Internet: bookstore.gpo.gov Phone: toll free (866) 512–1800; DC area (202) 512–1800
Fax: (202) 512–2250 Mail: Stop SSOP, Washington, DC 20402–0001

C O N T E N T S

WITNESSES

APPENDIX

"PROMISES MADE, PROMISES KEPT: ARE INTERNATIONAL TRADE AGREEMENTS REALLY INVESTMENT AGREEMENTS?"

WEDNESDAY, AUGUST 1, 2001

U.S. SENATE,
COMMITTEE ON COMMERCE, SCIENCE, AND TRANSPORTATION,
Washington, DC.

The Committee met, pursuant to notice, at 9:35 a.m., in room SR–253, Russell Senate Office Building, Hon. Ernest F. Hollings, Chairman of the Committee, presiding.

OPENING STATEMENT OF HON. ERNEST F. HOLLINGS, U.S. SENATOR FROM SOUTH CAROLINA

The CHAIRMAN. Good morning. The hearing will please come to order. Mr. Chairman—I still call him Chairman—it is good that you and I are here, because we can always agree. On the last hearing we went from side to side and what I was doing was recognizing those who had just come in, in disregard of those who had been waiting for an hour-and-a-half. So whether they are Republican or whether they are Democrat, unless you object, we are going to recognize them as they come in.

Senator MCCAIN. However you would like to, Mr. Chairman, is fine with me.

The CHAIRMAN. I think that is a fair way to do it, because the question was raised at that time.

Mr. Chairman, we welcome you today back from your travels and getting on to what I consider the most important subject really facing the U.S. Congress. For example, we were just reading here that—this is in the morning *New York Times*—since 1995, the U.S. current account deficit, the difference between what we buy from foreigners and what we sell to them, has quadrupled to an astonishing $450 billion.

It goes without saying that this is the biggest such deficit in world history. Startlingly, it is a fact that at 4.5 percent of the GDP, the U.S. current account deficit is a bigger share of the economy than the deficits Indonesia and South Korea had on the eve of the 1997 Asian fiscal crisis.

I notice, and I commend you for it, Mr. Secretary, in your appearances from time to time you introduce yourself as having met a payroll, having executed a business plan. Let me speak in a similar fashion.

I was admitted to practice before the U.S. Customs Court, practicing before Judge Paul Rayall of New York back in the 1950s. I

testified before the old U.S. Tariff Commission before it was changed into the Trade Commission, when Tom Dewey chased me around the hearing room. That was almost 40 years ago.

Thinking of it, the big issue is the Free Trade with the Americas Initiative by the Bush Administration. I do not want to sound like Al Gore, but I invented free trade with the Americas 40 years ago when I went as a Governor—I was the first Governor to go down to Latin America to promote trade. So I am a very strong believer in trade.

The point that I am trying to make is, with this experience, we know that Fast Track is not necessary. Only yesterday, the House of Representatives approved the trade treaty and agreement with Jordan without Fast Track. I remember President Clinton during his 8 years entered into some 234 trade agreements. We in turn approved, without Fast Track, the Chemical Weapons Treaty; we approved the sub-Sahara with all the nations in Africa; we approved, without Fast Track, the Caribbean Initiative. If they bring them over, we will be glad to support—and I have said so publicly prior to this hearing—not only the Jordan agreement, but the one with Vietnam.

So we can act, and in my 34 years that has been the better approach, because I have found that Fast Track really causes problems.

I will never forget the debate we had back in 1993-1994 on NAFTA with Fast Track. At that time, we submitted that the proper approach—and I will put an article in the record at this particular time that we wrote for Foreign Policy—it was the Common Market approach that was used in Europe.

The Europeans found that Fast Track was a mistake, that you had to first build the infrastructure of a country before you could really get into an effective and fair trade agreement. Namely, you had to have free elections. I can hear my former colleague, Senator Moynihan: "How can you have free trade when we do not even have free elections. You have got to have free elections, you have got to have property ownership rights, you have got to have labor rights, a respected judiciary; build in the infrastructure for health and, yes, for safety."

We had not built that in. I only met yesterday with Dr. Derbez, who is the Economic Minister from Mexico. He and I went over what is the so-called Murray—it is bipartisan—Murray-Shelby amendment. I said: "Mr. Minister, I want you to name one thing in these particular requirements that have got to be worked out that is not required of the American truck driver? If it is not required of ours, out it goes."

That was the approach we in the Senate used. In other words, over on the House side, they were rather arbitrary; they just said, "We are going to cut off any money."

The President announced that he was going to open up the border on January 1, and they more or less said, "the heck you are, and we are going to cut off any money to do that." Well, that is not any way to implement NAFTA. In order to do it we said, "here, the border can be opened up until, until, until," and we outlined these things that are required for safety of our own truck drivers.

We have got a lot of work to do also. In other words, there are only 2 of the 27 stations that are ready to receive trucks and we do not want the backups. We have got to put in the weigh stations, all those kind of things. One is, for example, we inspect, like the Mexicans. They inspect our apples up in Seattle right now, we inspect and find out that they have got the right safety requirements down there. Then when they present the sheet of paper at the border we know it is credible, and it facilitates.

So you have to build up the infrastructure. We found out it not only caused the problems, but it was absolutely a failure in the sense that NAFTA—I have heard the witnesses come before this Committee time and again, but they told us that we were going to promote trade. We went from a $5-billion-plus balance of trade in the United States with Mexico to a minus-$25-billion. We were supposed to get 200,000 jobs; we lost 500,000 jobs.

The worker in Mexico, he has got more jobs, but he is taking home less pay, 8 percent less pay. Just this last week, I quote Presidente Fox: “It is not possible to solve the migration problem,” Fox said, “if we do not solve the gap where a worker in Mexico earns $5 a day and a worker in the United States makes $60 a day.” That brings into sharp focus how the matter of trade is really a reconciliation of standards of living. What we must do is remember that Fast Track and NAFTA did not work with respect to the immigration problem. I hear what Constantine, head of the DEA, said just before he left, it was worse than the drug problem.

The biggest opponent of Fast Track in the NAFTA agreement was none other than Jorge Castaneda, the foreign minister; and Aguilar, who is now the security minister. They were the ones who testified before this Committee by satellite until Escara down there cut them off.

As we understand your background and leadership in business, you should understand our background in working on this particular problem. As you say, you must be accountable to the shareholders. I am accountable to the voters, and Article 1, Section 8, of the Constitution says that the Congress shall regulate foreign commerce. We would not ask the President to give us authority to approve or veto, and he should not be asking us to really regulate the free trade and regulate commerce itself.

I was the biggest opponent, in a way, of NAFTA. But I am the biggest proponent today to see that it works, I can tell you that, because they are our neighbor. If I had my way, I would start, as I discussed with you, a Marshall Plan down there to immediately try to build that infrastructure. That is what Castaneda, Aguilar, Presidente Fox and all of them believe in, and I am convinced of it now, having met with the economic minister yesterday afternoon.

Let me yield to Senator McCain.

STATEMENT OF HON. JOHN McCAIN, U.S. SENATOR FROM ARIZONA

Senator McCAIN. Thank you, Mr. Chairman. I would like to commend you for continuing the dialog on this important issue. While the Members of this Committee may not always agree on trade related issues, I believe we all benefit from this discussion.

As we move toward a global economy, with countries increasingly interlinked, trade agreements have ascended to center stage and the United States cannot afford to wait in the wings. I realize that critics of trade agreements and U.S. investment abroad fear the exportation of American jobs and the abuse of nations with cheap labor and low environmental standards. Skeptics will always find examples to support their arguments.

The reality, however, is that trade agreements enable domestic expansion, reduce foreign barriers to U.S. products and industries, and ensure that the United States remains competitive in the international marketplace. U.S. foreign direct investment abroad flows to developing economies rather than underdeveloped. Economic expansion, maintenance of global stability, enhanced security, and improved multilateral relationships are merely a few of the numerous benefits of foreign trade.

Whether we like it or not, we live in a global economy, and today U.S. businesses, workers, and consumers rely on the global economy for job markets in which to sell goods and services and affordable products to consume. Today 1 in every 3 acres of U.S. farmland is planted for export and more than 12 million U.S. jobs now depend on trade.

NAFTA provides an excellent example of the benefits of trade. Together, the Uruguay Round trade agreement and NAFTA increased U.S. national income by $40 to $60 billion a year.

We are all aware of many of the statistics, but since the signing of NAFTA, trade between the United States and Mexico has tripled. As of 1999, the U.S. Chamber of Commerce estimates that NAFTA was responsible for the creation of more than 685,000 new export-related jobs in the United States.

Mexico also experienced substantial economic benefits from NAFTA. Anyone who travels to northern Mexico can see the dramatic economic improvement in the conditions there in northern Mexico, and any Mexican businessperson or expert will tell you that it is a direct result of the economic benefits associated with NAFTA.

Since implementation, Mexico's GDP has increased at an average of 3.7 percent a year. Foreign direct investment has improved the lives of Mexican workers, who now earn 48 percent more than the average national wage from their work in foreign-owned subsidiaries.

The expansion of free trade promotes democratic values such as transparency, rule of law, protection of private property, and freedom of the press. NAFTA, for example, I strongly believe can be credited in part for Mexico's successful transition to democracy after 70 years of one-party rule.

I would like to applaud Secretary Evans for his efforts to expand trade and economic cooperation abroad, particularly in his efforts to promote trade negotiating authority.

Although part of a new administration, Secretary Evans is well versed in the issues surrounding the trade debate and I look forward to hearing his perspective.

This is not a new debate. It goes back to the founding of this Nation and will undoubtedly continue. Senator Hollings and I have had many debates on this issue and we will continue to have many

spirited discussions on this issue, albeit somewhat repetitious. I believe that as a country we must be globally engaged and commit ourselves to the expansion of free trade.

Now, Mr. Chairman, just for a second, since you brought it up, the issue of Mexican trucks. You and I do have a lot in common, including the fact that we both ran for President and we both failed. So neither one of us are President. The President of Mexico and the President of the United States have judged the language in the supplemental appropriations bill—an appropriations bill, I might add, when rightfully, this issue should have been addressed in this Committee—is in violation of the North American Free Trade Agreement.

Our opinions are important, but the people of Mexico and the people of this country have delegated the responsibility for this judgment to the President of the United States. The President of the United States' judgment is unequivocal. It is unequivocal that the language in that bill is discriminatory to Mexico. I can only speak for myself. I do not believe that anyone in the Congress is anti-Mexican or anti-anything.

But the effect of the language in the supplemental appropriations bill is discriminatory against Mexican business by not allowing them to do business in the United States, as we agreed to by a solemn treaty. That is why the President of the United States has threatened to veto this supplemental appropriations bill for transportation, which would harm, obviously, many important transportation projects throughout the country.

We have offered to negotiate. There are only four remaining issues that exist on this issue. Unfortunately, the authors and sponsors of the legislation have refused to negotiate. I have negotiated on a lot of issues around here, and come to agreement on some very serious ones, and I continue to be disappointed that there has been no movement in negotiation on this issue.

But the fact remains, the bill will be vetoed by the President of the United States, and that is not good for America nor good for Mexico, nor is it good for the perception that the Mexican government and people have about the United States and its willingness to conform with solemn treaties entered into between our two countries.

I thank you, Mr. Chairman.

[The prepared statement of Senator McCain follows:]

PREPARED STATEMENT OF HON. JOHN MCCAIN, U.S. SENATOR FROM ARIZONA

Thank you, Mr. Chairman. Once again, I would like to commend you for continuing the dialog on this important topic. While the Members of this Committee may not always agree on trade-related issues, I believe we all benefit from this discussion. Thank you for your perseverence on this matter.

As we move toward a global economy, with countries increasingly interlinked, trade agreements have ascended to center stage, and the United States cannot afford to wait in the wings. I realize that critics of trade agreements and U.S. investment abroad fear the exportation of American jobs, and the abuse of nations with cheap labor and low environmental standards.

Sceptics will always find examples to support their arguments.

The reality, however is that trade agreements enable domestic expansion, reduce foreign barriers to U.S. products and industries, and ensure that the United States remains competitive in the international marketplace. U.S. foreign direct investment abroad flows to developed economies, rather than underdeveloped. Economic

expansion, maintenance of global stability, enhanced security, and improved multilateral relationships are merely a few of the numerous benefits of foreign trade.

Whether we like it or not, we live in a global economy—and today, U.S. businesses, workers, and consumers rely on the global economy for jobs, markets in which to sell goods and services, and affordable products to consume. Today one in every three acres of U.S. farmland is planted for export, and more than 12 million U.S. jobs now depend on trade.

NAFTA provides an excellent example of the benefits of trade. Together, the Uruguay Round trade agreement and NAFTA increased U.S. national income by $40 to $60 billion a year.

From the time of NAFTA's implementation until very recently, the United States experienced the longest peacetime economic expansion in history. Unemployment fell from 7 percent to 4 percent. The U.S. gross domestic product grew by more than $2 trillion. And real family income in the U.S. rose by an average of $2,500. Since the signing of NAFTA, trade between the United States and Mexico has tripled. As of 1999, the U.S. Chamber of Commerce estimates that NAFTA was responsible for the creation of more than 685,000 new export-related jobs in the United States.

Mexico also experienced substantial economic benefits from NAFTA. Since implementation, Mexico's GDP has increased at an average rate of 3.7 percent a year. Foreign direct investment has improved the lives of Mexican workers who now earn 48 percent more than the average national wage from their work in foreign-owned subsidiaries. NAFTA sparked a Mexican export boom, credited with the creation of 3.5 million jobs since August 1995.

The expansion of free trade also promotes democratic values such as transparency, rule of law, protection of private property, and freedom of the press. NAFTA, for example, I strongly believe, can be credited in part for Mexico's successful transition to democracy after 70 years of one-party rule.

I would like to applaud Secretary Evans for his efforts to expand trade and economic cooperation abroad, particularly in his efforts to promote trade negotiating authority. Although part of a new administration, Secretary Evans is well versed in the issues surrounding the trade debate, and I look forward to hearing his perspective.

This is not a new debate. In fact, it goes back to the founding of this Nation, and will undoubtedly continue. Time and time again we as a Nation are faced with the choice of engaging in global affairs, or retreating within our own borders. I believe that as a country we must be globally engaged, and commit ourselves to the expansion of free trade.

I hope that as a result of this hearing, we will all come away with a better understanding of the greater issues involved.

The CHAIRMAN. Mr. Secretary, just a minute. Lots of times up here in the Congress, the cart gets before the horse. We had set hearings on Mexican trucking, but when the President announced that the border was, ipso facto, going to be opened without regard on January 1, that put the House into action. The appropriations bill that the distinguished gentleman refers to came over from the House side already with the bar, so we had to deal with it in the appropriations bill. The gentleman knows that.

What we did then is we worked as an authorizing committee with the Appropriations Committee and, totally bipartisan, unanimously reported out of the Appropriations Committee. So this is not an arbitrary thing.

Otherwise, I can tell you right here and now that I have read the arbitration thing. I did not know we were going to be debating that this morning, but the arbitration panel referred to safety. Presidente Fox's representative was in my office yesterday afternoon. He agreed to it, we both have to adhere to safety requirements. When I asked him, I said, "now you have got your team here"—he had three other people with him. I said: "You just name it, or when you leave, just work it out and find anything in there that is not required of our own truck drivers. I want to know about it and I want to make a motion to knock it out myself."

So that is where we are.

Senator Allen.

Senator MCCAIN. Mr. Chairman, why do we not mark up a bill? Why do we not mark up a bill through this Committee next week? I will be more than happy to join with you and pass a bill through the authorizing committee, which is the appropriate way to legislate in this Congress.

The CHAIRMAN. Because we are going to pass a bill this week before we leave.

Senator Allen.

Senator MCCAIN. You ain't going to get it passed.

Senator ALLEN. Senator McCain, you can use some of my time.

STATEMENT OF HON. GEORGE ALLEN, U.S. SENATOR FROM VIRGINIA

Senator ALLEN. All of this is very important and let me just say, I am not going to get into the debate, although I will say that I generally agree with the views expressed by Senator McCain on this matter.

Now, on the matter of trade——

The CHAIRMAN. Your time is up.

[Laughter.]

The CHAIRMAN. Goodbye.

Senator ALLEN. I voted with you on a few of those amendments.

The CHAIRMAN. Excuse me, Senator Allen. I thank the Governor. He is a former Governor. We get along together.

Senator ALLEN. Mr. Chairman, let me start this way, then.

Congratulations on this wonderful hearing that you are having here today and the series of hearings that you have been having over the last month on the issue of international trade. I think it is very important that we all discuss our perspectives and also learn and determine what we need to do.

I am very happy, of course, to see Secretary Evans here and look forward to his remarks, and I am sure he will digest the comments from this Committee in moving forward.

I believe, Mr. Chairman and Ranking Member Senator McCain, that international trade can improve lives. I think it can create more job opportunities here. I also think it can secure peace, because when there is more economic ties and commerce then there is less of a chance of disruption, and people generally in business, they do not like disruptions. So even indirectly, I think it is helpful for peace.

I am a strong supporter of giving the President the trade authority that he needs to expand our markets abroad. I think it means more opportunities for our businesses and enterprises, and I also believe it means good-paying jobs for our workers. I think trade promotion authority clearly is going to open up markets that have barriers to our services, our products, and our goods. I think it will ensure growth, especially in our high tech economic sector. I think it will help get other countries to the negotiating table, realizing that the President has the authority to negotiate a contract and not have somebody else change it too much.

I think it makes us a leader in world trade, which I think is important, because I think Americans can compete with anyone in the world. Now, there are some areas where it may be more difficult.

But just from my perspective as Governor of Virginia, Mr. Chairman, I know that we were looking at what the impact of trade is. Virginia sold more than $10.5 billion worth of exports to nearly 200 foreign markets last year. The number of Virginia companies exporting increased 62 percent from 1992 to 1998. More than 79 percent of Virginia's approximately 4,700 companies that export are small and medium-sized businesses. There are an estimated 142,000 Virginia jobs that depend on manufactured exports and 1 out of every 7 manufacturing jobs in our Commonwealth of Virginia, which ends up being about 59,000, are tied to exports.

Now, Virginia benefits from exporting anyway even if the origination is not Virginia or the destination Virginia, in that commerce may be going through our ports. It may be something coming from Kentucky or West Virginia or Ohio or even parts from—I know very well that parts from Michigan for Voyagers going to Austria, we were able to get them to bring it through our ports in Virginia rather than having them go through the ports in New York and New Jersey.

We also found, while I was Governor, in analyzing this that the jobs, the pay is higher on workers who are involved in exporting by about 13 to 18 percent higher than the national average. We have about 6,000 citizens in our Commonwealth who hold jobs that are related to agricultural exports. Virginia reported an estimated $386 million in agricultural products exported in 1999.

Our exports, in particular as far as Canada and Mexico go, increased. 1999 was 90 percent higher than in 1993, prior to NAFTA.

Now, I am hopeful, Mr. Chairman, that in the midst of all these Mexican truck and transportation matters that somehow this week we will be able to modernize the Export Administration Act. That Act is outdated, it is outmoded. It expires on August 20, and it seems to me that it is not doing much at all, if anything, to protect our security, but the outmoded, outdated Export Administration Act is mainly harming our ability, especially technology companies, to be competitive in selling overseas, and those products or technologies are being sold by people from France or Germany or Japan or Korea or elsewhere.

Now, as Governor—you were talking about being Governor and leading trade missions, and that is one of the best parts of being a Governor, I think. You are in a position, you are the CEO of the State. You are able to sit there and give credibility to whichever businesses, large, small, or medium that come with you, and you also can strike a deal. You can close that deal with the CEO of a company.

My first year in office was 1994, and we went up to Canada and to Mexico. We wanted to take advantage of these open markets or opening markets. It was very helpful. When we first went up to Quebec, a small company called Radva that makes housing construction equipment, they secured a deal the first day and they did not care to go on to Toronto or anywhere else. They got what they wanted, a $5 million contract.

We went down to Mexico as well, and from that, we were able to help sell to the Mexico City police Ericsson secure radios or telephones for their security, their critical radio systems, and those were made in Lynchburg, Virginia. We got a $10 million contract

for a bearings company in Virginia when Mexico was trying to upgrade their rail system.

So it was very, very successful and there were others from it. But the point is that, over the years, we went on trade missions everywhere. We were all over, obviously to Britain and France and Germany several times, also to opening markets in Poland, Hungary, the Czech Republic, Sweden, Denmark, Austria, Korea several times, Japan several times, Egypt, Israel, Hong Kong, Taiwan, and elsewhere.

All of these really did pay off, and it was great for promoting our goods and products and services. In some of the more developed countries, it was mostly valuable in recruiting new investment and new jobs into Virginia. Just from Sweden, we had Volvo Trucks and Ericsson.

From Great Britain—I was just writing down notes as you were talking. From Great Britain, Drake Extrusion, Allied Colloids; France, we were able to get Jouan Medical Equipment; PGF, which is Porshay Industries; Framatome was already a French company in Virginia. Denmark, we were able to get Mersk Marine to move to Virginia. The Netherlands, Blueprint Automation; Germany, Siemens Steel, chain saws; Infineon, Klockner, Von Holtzpring Publishing, Muelbauer, to name a few; Maple Leaf Bakeries from Canada.

From Japan, we got Toshiba to build a several billion dollar semiconductor fabrication plant in Manassas; Tama Chemical, Wacco Chemical, Sumitomo, Torre, Yokahama Tires, Canon, Tokyo Electron, Upo Paper, Mitsubishi Chemical; Australia, RGC, industrial galvanizers; and others from Korea and Austria and other countries.

So I could go on and on, but the point is Virginia is benefiting mightily from international trade, whether it is our products going out and services or goods, but it is also benefiting from the fact that these countries, especially those who have a history of freedom and the rule of law and private property rights, have the capital to invest and come into our country.

I know South Carolina is a fierce competitor, and South Carolina, with your leadership that you started there and carried on by Carol Campbell and others, has done a great job in recruiting Japanese companies and German companies and others from all around the world, and that benefits the people of our respective States.

Now, I do want to say this. Trade and international competition, when you are looking at a bottom line in a business sense, is a net plus, but there are also negatives.

International competition can cost jobs. That is recognized in NAFTA. Mr. Chairman, I mentioned this at an earlier hearing and I am going to mention it again, that the Transitional Assistance Act which was put into place to help people transition when they are unemployed because of international competition, is a good idea for retraining.

I saw in South Side Virginia, the Martinsville, Henry County area, a lot of people, thousands of people who lost jobs, textile business. Toltex was the particular company.

It was, to me, like a natural disaster, like a flood hit, but it was an economic disaster.

I think that as we go forward with any trade legislation, Mr. Secretary, that there ought to be an understanding that a lot of these folks, all of them, are good, hard-working, loyal employees and through no fault of themselves they have lost the money. So I would like to see something. Give them home preservation loans, give them a bridge loan, so that they do not lose those jobs. I think that ought to be a part of it.

Both the leading folks say that we want to hear from you, so with that I look forward to hearing your remarks. You have an ally in me and I hope to work with you in the future.

Thank you, Mr. Chairman.

The CHAIRMAN. Very good. Thank you, Senator.

Secretary Evans, we would be delighted to hear from you, sir.

STATEMENT OF HON. DONALD L. EVANS, SECRETARY, DEPARTMENT OF COMMERCE

Secretary EVANS. Mr. Chairman, delighted to be here.

Mr. Chairman, nice to see you. Senator Allen, thank you very much.

Mr. Chairman, I am not sure we agree on TPA. I am going to do my best to persuade you that TPA is something that is very important for this President and this country to lead America, lead the world in trade. But it is always a pleasure to be here and if I might, I would like to have my written testimony——

The CHAIRMAN. Your statement in its entirety will be included in the record and you can summarize it or deliver it in full.

Secretary EVANS. Thank you very much. I would like to do that. Thank you, Mr. Chairman.

President Bush and I agree that trade is the key to increasing prosperity and extending freedom, equality, and security around the world. It is a moral imperative. That said, I never lose sight of the fact that trade is, above everything, a bread-and-butter issue for all Americans. With 98 percent of global gross domestic product and 95 percent of humanity outside of our borders, it is clearly in our interest to open foreign markets to American exports.

As you have pointed out previously, Mr. Chairman, both trade agreements and trade barriers are about investment. I understand your concern and the concern of other Members of the Committee and Congress that trade agreements might become a vehicle for encouraging investment abroad. I will come back to that point in a moment.

I also want to make sure we take into account the opposite perspective, that removing foreign barriers to trade can also eliminate the incentive to invest abroad to avoid high tariffs. The net result is that our firms can maintain investments and production here, because they can gain access to foreign markets by exporting.

The vast majority, nearly three-quarters, of total U.S. direct investment abroad is in other developed countries that have high labor and environmental standards and enforcement.

What that underscores this is that American capital flows to where there is a positive and secure investment environment, one that provides the rule of law and acceptable rate of return, rather than one driven by lower labor standards and lax environmental enforcement.

U.S. business tends to take its labor and environmental standards abroad when investing, thus raising the bar in countries where domestic standards are lower.

In addition, our exports often follow U.S. direct investments abroad. Studies have shown that for every $1 in overseas investment, an additional $2 in exports to that market tend to be generated. In this regard, we have to get back in the international trade game and break down barriers to U.S. exports and improve job opportunities for American workers.

To do that, Congress and the President need to reach agreement on the scope and goals of trade negotiations. The vehicle to make that happen is Trade Promotion Authority, and the sooner the better. As President Bush has observed, free trade agreements are being negotiated all over the world and we are not a party to them. There are over 130 preferential trade agreements in the world today. The United States belongs to only two. Our competitors are busy signing deals while our negotiators sit on the sidelines, and these deals are placing us at a competitive disadvantage.

Both strengthening the President's hand in negotiations and reinforcing the constitutional role of Congress are essential to a successful American trade policy, one that serves the interests of all Americans.

I understand, as you do, if we do not enforce our current agreements we cannot expect support for further negotiations.

I have made compliance and enforcement the highest priority for all units in international trade administration.

Mr. Chairman, I want to thank you for your support for the compliance initiative and assure you that we have been moving ahead. In terms of compliance, our emphasis is on problem-solving and results. I am also committed to aggressively investigating allegations of subsidies and dumping under our trade laws. American workers and farmers can truly be dispirited by the belief that they are not competing on a level playing field.

We are also acutely aware of the fact that for our economy to fully benefit from new market openings, we need to expand the base of exporters, and that means including every sector of our economy, especially our small businesses. This requires the coordinated effort of all Federal agencies involved in export promotion and trade development.

Fortunately, we have the right management tool in place, the Trade Promotion Coordinating Committee, which comprises 19 agencies. The Coordinating Committee works on behalf of small businesses by coordinating government export promotion programs so that small companies can access them more easily.

Mr. Chairman, we need to engage in a dialog that will help us move forward as a Nation, with the full support of Congress, for our efforts to open new markets for American goods, services, and ideas. Americans have always been at the forefront of change and progress and we have always prospered as a result. That is what has made us such a forward-looking Nation. I believe we can continue to lead in a world that is more active than ever in trade and commerce, and I truly believe that we should do this in a way that provides opportunities to all American workers, business owners, and families.

Thank you for your time and I will be happy to answer any questions that you might have.

[The prepared statement of Secretary Evans follows:]

PREPARED STATEMENT OF HON. DONALD L. EVANS, SECRETARY, DEPARTMENT OF COMMERCE

Thank you, Mr. Chairman, Senator McCain, and Members of the Committee, for inviting me to testify before the Senate Commerce Committee on how to ensure that Americans receive the benefits from the trade agreements we negotiate.

Mr. Chairman, I would like to discuss our ideas about establishing a new American trade agenda to serve the interests of all Americans. I will address the need to expand our exports—to benefit our businesses, our farmers, our workers; the need to monitor compliance; and the need to support export promotion activities to "fill in" behind our negotiations. I am interested in the Committee's view on an agenda to serve that purpose. That is, I am here today as much to listen as to testify.

EXPANDING ECONOMIC OPPORTUNITIES FOR ALL AMERICANS

President Bush and I agree that trade means considerably more than just economic growth, more higher-paying jobs, and a rising standard of living in America. Trade is ultimately about freedom. It is the freedom for America's farmers, entrepreneurs, and workers to pursue their own economic destiny. And, as the President has said, trade also encourages those habits of liberty that form the foundation of democratic self-government. Trade and open markets allow men and women around the world to pursue their own destiny, rather than depending on the hand of government to determine their future. That's why President Bush calls free trade a moral imperative. Mr. Chairman, freedom is our most important export.

Importance of Expanding Exports to the U.S. Economy

That said, Mr. Chairman, I never lose sight of the fact that trade is, above all, a bread and butter, kitchen table issue for all Americans. Beyond the moral arguments and beyond statistics, trade has real meaning for and a real impact on real people. What that boils down to is whether our trade policies are expanding economic opportunities for U.S. farmers, workers, and firms here at home and abroad. That, in turn, depends on opening new markets for U.S. exports.

The United States, I am pleased to say, remains the world's largest exporter, with U.S. exports representing a 12.7 percentage point share of total world exports of manufactured goods. U.S. exports accounted for nearly one-quarter of our economic growth during the past decade. More than 20 percent of the goods produced in the United States are exported, and more than 200,000 U.S. firms rely on exports for some portion of their business. With 78 percent of global gross domestic product and 95 percent of humanity outside our borders, we must continue to open foreign markets to American exports.

Last year, U.S. exports of goods and services were equivalent to 11 percent of gross domestic product. U.S. export trade has expanded even faster than the overall U.S. economy. U.S. exports increased from $57 billion in 1970 to $1,069 billion in 2000, an increase of over 10 percent per year. We estimate that some 12 million U.S. jobs are now supported by exports, and these jobs pay up to 18 percent more than the national average.

Equally important, exports make up a growing share of the markets served by American small and medium-sized businesses. Those businesses create three out of four jobs in America, account for one-half of the annual U.S. gross domestic product, and represent 97 percent of all U.S. exporters. To stay at the forefront of innovation, U.S. small and medium-sized businesses need access to foreign markets and a level playing field globally.

The growth in trade as a factor in the U.S. economy mirrors the importance of trade globally. Trade as a percentage of the world economy has grown 16-fold since the creation of the General Agreement on Tariffs and Trade in 1947. Estimates of the increase in global growth that would result from a new round of World Trade Organization negotiations run as high as $600 billion. Both the growth in world trade and the process of writing the rules that will govern trade relations will go on, with or without us.

Given the competitiveness of the U.S. economy, the growth in world trade and the potential reduction of barriers to U.S. exports could open a new market for U.S. exports. But, to realize that potential, the President has to be able to take a seat at the negotiating table. It is not in our national interest to let the rest of the world set the rules of the road that will govern our trade. When the rules of the road are

set by others, they will create, rather than remove, barriers to our exports and put American exports at a competitive disadvantage. And, in the end, that means less investment, slower economic growth and fewer job opportunities.

Relationship of Trade and Investment

As you have pointed out previously, Mr. Chairman, both trade agreements and trade barriers are about investment. I understand your concern and the concerns of other members of the Committee and the Congress that trade agreements might become a vehicle for encouraging investment abroad solely as a means for lowering a company's costs and then exporting back to the United States.

First, let me say that trade and investment are not either/or propositions. Our experience throughout the post-war period is that trade and investment grow together. Europe and the United States have invested heavily in each other, yet trade has also grown rapidly. That said, we as a Nation have been concerned about trade barriers and investment rules that are intended to force U.S. firms to invest abroad rather than export and/or to have to export a large part of the output of their foreign investments back to the United States.

For example, when U.S. automobile exports face high tariffs of 35 percent in Brazil (as opposed to the 2.5 percent tariffs Brazilian autos face here), it creates an artificial incentive to invest in Brazil behind that high tariff wall. That means that Brazil gets both investment and jobs that would otherwise go to the United States. Eliminating those tariff barriers would allow American companies to enter the Brazilian market by exporting, and the investment and jobs would stay home in the United States.

In other cases, countries impose investment requirements or provide investment incentives that encourage U.S. firms to invest abroad as a condition of access to their markets. Those requirements or incentives are often coupled with the obligation to export a significant share of the new facilities output. The net effect of these "trade-related investment measures" is to shift investment abroad and reduce job opportunities in the United States.

Elimination of those requirements or incentives, together with tariff reductions, allows U.S. firms to export, thereby keeping investment and jobs here at home. For example, when Chrysler was deciding where to build the Durango, now one of the hottest selling vehicles in the North American market, it was able to base its plant in Delaware, rather than having to build in either Mexico or Canada to gain access to those markets. This is a good example of how trade liberalization under the North American Free Trade Agreement (NAFTA) has affected both trade and investment.

The numbers on investment tend to bear out what one would expect from the elimination of trade barriers abroad. Over the last 5 to 10 years, while the tariff cuts under the NAFTA and the Uruguay Round took hold, the United States has continued to see a strong inflow of foreign investment generally. In fact, the United States has steadily run a capital account surplus since 1975. Statistics on foreign direct investment (FDI) reinforce the same basic message: the United States remains both the largest exporter and the largest recipient of FDI.

In other words, since the implementation of the NAFTA and the Uruguay Round and the elimination of significant barriers to U.S. exports, we have seen more foreign direct investment in the United States than we have seen U.S. direct investment abroad. What that means in practical terms is that eliminating barriers to U.S. exports can have a real impact on the level of investment and the number of jobs created here in the United States. While eliminating those trade barriers is not the only thing that makes the United States an attractive place to invest, it certainly has been a strong contributing factor.

Need for Trade Promotion Authority

Mr. Chairman, we have got to get back into the international trade game if we are to break down barriers to U.S. exports and improve job opportunities for American workers. President Bush has observed that, "Free trade agreements are being negotiated all over the world, and we're not party to them." There are over 130 preferential trade agreements in the world today. The United States belongs to only two.

Our competitors are busy inking deals while our negotiators sit on the sidelines, and these deals are placing us at a competitive disadvantage. For instance, a U.S. company exporting a tractor to Chile must pay a $25,000 tariff. If that U.S. company moved its factory to Brazil and exported a tractor to Chile, it would pay a $15,000 tariff. But, a Canadian company exporting a tractor to Chile pays *no tariff at all* because Canada has a free trade agreement with Chile. What that means is

that the Canadian company is going to get the sale, and the investment and jobs that go along with producing that tractor.

The President has made clear that he intends to press forward wherever we can to expand trade and economic opportunities for all Americans. We want to be prepared to take action where the opportunities arise and to ensure that our exporters gain their fair share of the new export markets those agreements may create. To do that, however, the Congress and the President need to reach agreement on the scope and goals for our trade negotiations. And, the vehicle for reaching that agreement is Trade Promotion Authority (TPA).

It has been argued recently that TPA is not necessary now, that it is only needed at the end of a negotiation to implement the deal. My own view is that TPA is just as important at the beginning of a negotiation as it is at the end. That is because TPA represents something of a contract between the Congress and the President on the scope of negotiations and the goals we should pursue at the negotiating table.

With TPA in hand, the President can face our trading partners with the full backing of Congress. And, our trading partners cannot mistake the importance of Congress' role in setting the agenda for such talks, as well as its role in approving and implementing any eventual bargain. In my view, that both strengthens the President's hand and reinforces the constitutional role of the Congress in the trade policy process.

Both strengthening the President's hand in negotiations and reinforcing the constitutional role of the Congress are essential to a successful American trade policy—one that serves the interest of all Americans. Given what is at stake in terms of economic opportunity, the time to renew the contract between the Congress and the President is now. The United States has historically played a leadership role in international trade, constantly pushing for more freedom, more opportunity, and more fairness in the global marketplace. It is time America got back in the game.

COMPLIANCE AND ENFORCEMENT ARE KEY

Mr. Chairman. I understand—as do you—that a second element is needed to ensure that American farmers, workers and firms benefit from an aggressive American trade agenda. The process here in the United States cannot end with the negotiation of an agreement and its implementation by the Congress. If we do not aggressively enforce our current agreements, we cannot expect Americans to support further trade negotiations. That is, promises made must be promises kept.

In the end, it is about trust. The ability of the Congress to trust that the President will make use of Trade Promotion Authority in a way that works for all Americans and the ability of the American people to trust both the Congress and the President to defend their interests. That trust ultimately depends on our ability to ensure that the United States gets what we bargained for under existing and future trade agreements.

I believe in keeping a bargain when I make one. Since my confirmation hearing before this Committee in January, I have made compliance a top priority at the Commerce Department. Mr. Chairman, I know the important role you played in focusing the Department's compliance efforts in the past, and I want to provide you with the strongest possible assurance that we will follow through.

Making Compliance and Enforcement a Priority

I have made compliance and enforcement the highest priority for all the units within the International Trade Administration, so that our commercial officers at home and overseas, as well as our industry analysts and desk officers in Washington, work together to enforce our trade agreement rights. Our emphasis is on problem-solving, and we have cast a wide "net" in that effort. Rather than simply waiting for problems to come to us, the Department conducts extensive public outreach programs to ensure that American business understands the benefits of trade agreements that they are due and the resources available through the Commerce Department and other governmental agencies to enforce them. We have a Compliance Liaison Program with trade associations and local business export councils to facilitate communication and prompt action on compliance issues. We also conduct routine surveys of our private sector Compliance Liaisons to learn about trade barriers and compliance problems their industries are facing.

While much of the attention focuses on ITA and its Market Access and Compliance (MAC) unit, I have made clear that trade agreements compliance is everyone's job, not only in ITA or MAC, but throughout the Department. ITA coordinates a biweekly Compliance Coordinators meeting, including representatives from all relevant Commerce Department agencies, to promote the sharing of their expertise on compliance issues facing the Department and American exporters. Thus, the National Institute of Standards and Technology, for example, may help ITA analyze

whether a country is abiding by the WTO Agreement on Technical Barriers to Trade when it proposes a new standard or a testing and certification requirement that affects U.S. exporters. Similarly, the Patent and Trademark Office assists ITA in determining whether the actions of certain countries are consistent with the WTO Agreement on Trade-Related Aspects of Intellectual Property Rights. ITA and the National Telecommunications and Information Administration (NTIA) work together to promote pro-competitive regulatory environments in foreign telecommunications markets, including monitoring and enforcement of commitments made in the WTO Agreement on Basic Telecommunications Services. ITA relies on NTIA for its expertise on the telecommunications policy in the United States so that these principles can be effectively advocated with foreign governments.

The most important point is that it works. Let me offer a few recent examples.

- In May, we helped a Virginia company referred by Senator George Allen's office to gain access to the Canadian market for agricultural equipment.
- In June, after inquiries initiated by our Compliance Team, Taiwan announced that it would recognize National Marine Manufacturing Association certification for U.S. recreational water craft exported to Taiwan. U.S. companies can now sell pleasure boats to Taiwan without having to undergo additional and costly inspections and will no longer be required to make modifications to their boats to meet Taiwan-specific requirements.
- We worked with a small Oregon manufacturer of bicycle trailers that was concerned about a proposed German regulation requiring brake systems for its bicycle trailers; our team worked closely with the company to convey to German officials our industry's technical comments and concerns with the safety implications of the proposed amendment. These efforts proved successful, and, in early July, the German authorities agreed to drop the regulation, allowing the company to continue to enjoy increased sales to Germany, its largest export market.

As one of my first actions as Secretary, I expanded our compliance liaison outreach to include the Congress. I asked all Members of Congress to identify a staff person to work with our Compliance Center to refer constituent market access or compliance problems. If staffs are not already working with us on this effort, I hope they will. The Trade Compliance Center also maintains a "Trade Complaint Hotline," a service that allows U.S. exporters, especially small and medium-sized firms, to file market access and trade agreement complaints online.

We also learn about potential problems from all different parts of the Department. Sources include the worldwide network of the Department's Commercial Service and Export Assistance Centers throughout the United States, our industry and country desks, and trade agreement specialists. For example, we received a complaint through our Columbia, South Carolina Export Assistance Center from a small company that was unable to sell its chemical product in Sweden because it was required to divulge proprietary information to a Swedish local government body. The Compliance team worked with the Swedish government to resolve the issue, resulting in an $8 million sale for the company.

Let me emphasize that our goal is to solve problems at a practical level. Once a problem is identified, a compliance action team analyzes it, develops a strategy and then applies compliance advocacy, in the form of calls, letters, area meetings between Departmental and foreign government officials—beginning at the staff level and working on up to me as needed. If, and when, that is not possible, we help build cases that USTR (U.S. Trade Representative) can litigate at the World Trade Organization or in other formal dispute fora.

Combating Unfair Trade Practices

While it does not always entail the enforcement of our trade agreement rights, I am just as committed to ensuring that we are aggressively investigating allegations of subsidies or dumping under our trade laws. There is nothing more dispiriting to American workers and farmers than to believe that they are not competing on a level playing field.

When our companies complain about unfair trade practices, our office of Import Administration (IA) is responsible for investigating the claims, ordering the imposition of offsetting duties, as well as seeking to eliminate the governmental interference or underlying distortions in the market that gave rise to the U.S. industry's complaint in the first place.

ITA's Import Administration unit also plays a lead role in monitoring trade agreements in the antidumping and subsidies arena. IA provides much of the substantive work on the annual report to the Congress on our trading partners' compliance with their subsidies commitments, as well as working within ITA and with U.S. Customs to ensure the vigorous enforcement of antidumping and countervailing duty orders resulting from their investigations.

In my view, these actions are not only consistent with our international obligations and the President's commitment to trade liberalization, but essential to them. By way of example, the security of America's softwood lumber industry and lumber jobs has been a key priority for me since I took office. In response to Congressional and industry concerns, on April 3, 2001, I initiated a Lumber Import Monitoring Program to keep track of import levels and detect destabilizing surges. We have been using a number of methods to ensure that we have the most current information available regarding the level of lumber imports. High-level Commerce officials have visited U.S. ports and have met with Customs staff in order to share information and educate them on our monitoring plans. As part of this plan, in order to get the most timely and accurate information, we secured the early release of preliminary softwood lumber data.

Following the expiration of the Softwood Lumber Agreement, my Department initiated two lumber investigations on April 23, 2001, to determine if softwood lumber imports have been unfairly subsidized and/or sold at dumped prices. We have teams of professionals hard at work ensuring that the investigations are conducted expeditiously and in full compliance with our unfair trade laws. You can be sure that we will enforce our laws vigorously where it concerns softwood lumber. We are taking a serious look at the allegations of critical circumstances and will take all steps to ensure effective and speedy relief.

I believe that the Congress well understands the necessity of finding solutions to address underlying market distortions. That is why, as part of the implementing legislation for the Uruguay Round Agreements, the Congress created the Subsidies Enforcement Office in IA to assist the private sector in fighting foreign subsidies. In addition, the Congress passed the Compliance Initiative for the fiscal year 2001 budget, providing compliance funding for several agencies, including the International Trade Administration's Import Administration and Market Access and Compliance units, which are expanding their activities. One key part of this expansion is the development of an overseas trade compliance team with staff in Beijing, Tokyo, Seoul, and Geneva.

Mr. Chairman, thank you for your support of the Compliance Initiative. I am committed to aggressive enforcement, and so is the President. He is asking us to go beyond investigating unfair practices. We seek to eliminate unfair subsidies, and the inefficient, excess capacity propped up by such subsidies. We are looking to find a way to get rid of the governmental interference and underlying distortions in the market.

EXPORT PROMOTION

Mr. Chairman, there is a third element to our approach to trade that is designed to reinforce what we do at the negotiating table and what we do in the way of compliance and enforcement. I am acutely aware that negotiating trade agreements, even with full compliance, will only take us so far. We need to "fill in" behind those agreements. For our economy to benefit fully from our efforts to open new markets, we need to expand the base of exporters and provide the promotional support they need to compete in the global marketplace, particularly our small and medium-businesses.

That, in fact, is an element that has been missing from our trade strategy to date and the President and I aim to rectify that situation. To take full advantage of the markets we open at the bargaining table, small businesses, in particular, need to get information, expertise, support and financing to do the deals that our agreements have made possible. This requires the coordinated effort of all of the Federal agencies involved in export promotion process.

Benchmarking Best Practices in Export Promotion

Fortunately, we have the right management tool in place—the Trade Promotion Coordinating Committee (TPCC), which was created by Executive Memorandum in 1990 and then adopted by the Congress in statutory form in 1992. The TPCC, which is comprised of 19 agencies, works on behalf of small businesses by working to coordinate government export promotion programs.

The TPCC has, for example, streamlined financing for small business, resulting in a quadrupling of the value of exports supported by the working capital programs of the Export-Import Bank and the Small Business Administration (SBA). Recently, the TPCC organized a series of seminars in Baltimore, Los Angeles and Chicago, during which officials from the Commerce Department, USTR, SBA, and the Export-Import Bank provided information to small firms about business opportunities arising out of recent trade legislation.

We have a plan for taking the TPCC back to its roots as a management tool by undertaking a benchmarking exercise that will help us better serve our small busi-

ness customers. Our goal is to ensure that we offer them world-class export promotion services in support of their efforts to take advantage of the new opportunities created by recent trade agreements.

As the Chair of the TPCC, I have received the commitments of the heads of the member agencies to undertake this innovative benchmarking review and have established a timeline for its completion. We will assess our customers' expectations and their level of satisfaction. We also will compare our business processes to those in other government agencies and the private sector to determine whether we are making use of best available practices. We intend to produce an interim report to the Congress at the end of September and provide a full report on March 30 of next year. This report will include recommended reforms of our programs and services.

It is more important than ever that our policy and promotion efforts on behalf of small businesses are coordinated and mutually reinforcing. Our goal is to provide the American people, and the small and medium-sized exporters in particular, the most efficient, strategically focused, well-coordinated and customer-driven programs possible.

Innovative Support for Small Businesses

Mr. Chairman, earlier I mentioned the importance of international trade to small business. Accordingly, I have placed a high priority on helping our small and medium-sized businesses benefit from our trade agreements. The Department of Commerce has a worldwide network of 1,800 employees who strive to help U.S. firms realize their export potential, with an emphasis on outreach to small and medium-sized enterprises.

We have Commercial Service officers posted in 160 locations in 85 countries abroad; they are our "eyes and ears" on the ground, sharing information with Commerce headquarters and our district offices. Our 105 U.S. Export Assistance Centers (USEACs) throughout the Nation offer export counseling, market research, trade events and international finance solutions to U.S. exporters. During fiscal year 2000, these centers counseled 12,955 U.S. companies, nearly all of whom were small and medium-sized.

The Commerce Department also has developed a number of high-quality tools to facilitate small and medium-sized enterprises (SME) exports. We offer free, online export finance Matchmaking and organize 1-day Creative Export Financing Seminars throughout the United States. Our Web portal—*export.gov*—consolidates export information into a single, customer-focused site.

This allows small businesses to quickly and easily identify sources of information on every stage of the export process—from finding a partner to getting paid. In addition, we have just added the capability to help SMEs transact international business online. Under this "BuyUSA" addition to our Web portal, U.S. exporters are matched with qualified international business partners and can also take full advantage of one-on-one export counseling from the local USEAC. Our Trade Information Center, with its toll-free telephone number, also provides counseling. During fiscal year 2000, the Trade Information Center handled 85,401 direct inquiries and had 645,284 Website hits—many of which came from small businesses.

From multi-billion dollar infrastructure projects to the strategic contracts for small businesses, our Advocacy Center fights to win deals for U.S. businesses and jobs for U.S. workers. Since its inception in 1993 to July 2001, the Advocacy Center recorded more than 160 advocacy successes for SMEs, totaling approximately $3.9 billion, with over $2.2 billion in U.S. content.

Mr. Chairman, it is clear that SMEs would be among the major beneficiaries of negotiations that reduce foreign barriers to U.S. exports. The number of SMEs that export merchandise soared from 108,026 in 1992 to 198,101 in 1998. These figures count only firms that export goods directly, and do not include suppliers whose inputs are exported in final products or services exporters. For example, nearly 200 companies in 27 states, representing about 75,000 other jobs, provide parts for the Case III MX Magnum tractor that is exported from the CaseNewHolland plant in Racine, Wisconsin.

TRADE NEEDS TO WORK FOR ALL AMERICANS

Mr. Chairman, we need to make our trade agreements work for all Americans. We need to engage in a dialog that will help us move forward as a Nation with the full support of the Congress for our efforts to open new markets for American goods, services, and ideas.

But, I would be remiss if I did not emphasize that it will take more than an active trade agenda, solid enforcement of trade agreements, and export promotion to succeed in the global marketplace. In the end, we need to make certain that America remains a place in which individuals want to invest their time, their talent, and

their capital. That will require a commitment to get the economic fundamentals right and ensure a constantly improving quality of public education not only for our children, but for those already in the marketplace. It will also require a sustained commitment to help those affected by the economic adjustment that invariably attends changes in our economy.

I look forward to working with you, Mr. Chairman, and the Members of the Commerce Committee to address those challenges as well. Thank you for inviting me to provide our views on trade and I welcome your questions.

The CHAIRMAN. Mr. Secretary, you note, as you did before the Finance Committee, that everybody is getting trade agreements everywhere and we are just being left behind. Of course, that is not the case. The situation is that we have already entered into the World Trade Organization with 124 countries, whereby at the time Secretary Cantor was saying this agreement gives us the level playing field we have sought in trade. For the first time, all the nations of the world will be signing onto the same set of trading rules, rules that are modeled after and shaped by our commitment to open markets and expanded trade. There will be no free riders.

Now we have Vietnam, Jordan. We just got sub-Sahara. We are making trade agreements. Like I say, President Clinton had 234. So we are not being left behind.

But mentioning that office, and that is why we got it—that is a recent office, because I have watched the history of this thing. I remember way back we found out that this Committee, Commerce—it used to be the Committee on Interstate and Foreign Commerce—since we were not doing the job, Senator Pastore over on the Finance Committee put in the Special Trade Representative.

In the last administration we put in the Office of Compliance. Why did we do that? Because we look right here, this "Foreign Trade Barriers" put out by the Special Trade Representative's office. That thing gets bigger and bigger. There are 68 pages in here of non-compliance by Japan. We can go down all of the countries.

So I am finding out that I am making more and more agreements and getting less and less. In fact, I have gone from, even in agriculture, way down now. I am losing out in agriculture. Someone mentioned automobiles a minute ago with Mexico. I have got a billion dollar deficit in the balance of trade in automobiles alone with Mexico.

I find out that, as you would say before the jury, the weight of the evidence, this is it. You folks put it out. That is your administration, and here it is. That is our big problem. We keep getting Secretaries and others coming up and telling us what a grand thing it is, and we keep losing out.

I have lost 42,100 textile jobs since NAFTA started down there to Mexico. They are closing down and all going out of business.

So we cannot just stand by and continue with the same litany that we have got compliance and it is a wonderful thing and everything of that kind.

What did you say about all of these violations here?

Secretary EVANS. Well, Senator, you know, when you enter into trade negotiations with any party around the world I think you have to—there are three thoughts, there are three principles that you ought to think through and be conscious of. One is make sure that you do your best, your very best effort in negotiating on behalf of the American workers and American businesses.

But once that agreement is signed, then you have to make sure that it is enforced and that all parties are compliant.

You raise a very valid point. I mean, when I look at areas of compliance I get concerned. It has been one of the areas that I focused on just this past couple of weeks, is the area of trans-shipments.

I listen to the fact that we do have a trans-shipment problem and the fact is, there are goods being shipped from one country to another country and a label put on them, and then the goods are shipped into America, and the Customs will catch that plant or country that violates the agreement and then we get it into our Justice system and there is no enforcement, there is no follow-through.

So when it comes to compliance, I do not think there is anything more important than making sure that when we sign agreements all parties understand that they are going to comply with the agreements. We ought to have the teeth and we ought to have the resources, and I thank you for adding the resources in the Department of Commerce. I know in the last budget you added $12.8 million, and we are in the process of adding 65 community officers in our trade community sector, which will be helpful.

But it is an area that is very important to us and we ought to be focused on it. I talked to Attorney General Ashcroft about this whole area of trans-shipments. I mean, the fact that we have laws in place and cannot enforce them and do not hold people in compliance is disturbing to me.

So I hear what you are saying. I mention two points in terms of, first, we have got to make sure we do a good job at the negotiating table and negotiate a good, sound agreement on behalf of the American people, and then we have to make sure these agreements are enforced. Then we also have to make sure we follow up with trade development and we make sure that we can open up markets for our small and medium-sized businesses.

But compliance is very important and we have added some resources to that area. Maybe we need to add some more. But I do not think that ought to prevent us from moving ahead with opening up markets around the world.

The CHAIRMAN. That is the point. We are trying to open up the markets. We have not opened up with Japan. This is just a few years ago, the same edition by the Special Trade Representative. Incidentally, this is a bipartisan complaint that I have. I could not get the Clinton Administration—and I am glad to have your testimony this morning that we are going to start enforcing it.

But you can see in the last few years it just doubled in size. In other words, I am getting more and more agreements, less and less compliance. We are not into Japan yet, 50 years later. Somehow we ought to learn that market forces operate. In other words, the day of the blooming aircraft carrier and atom bomb is gone. Market forces.

China: we had an agreement in 1989 to investigate them on human rights. The Chinese went all around into Africa and down to Australia and everywhere else and we have never had a hearing, and just 3 months ago we got kicked off the Human Rights Commission in the United Nations. Market forces operate.

We find Secretary Powell, who has just returned, like you, from Russia. He was trying to get them, admonishing them, the headline this morning, to please live up to their agreements. But we keep on hearing this thing and that is our frustration, because it gets— you know, there is an old saying in your back yard and mine: "there is no education in the second kick of a mule." We have been kicked around here for 50 years.

Let me yield to Senator McCain.

Senator MCCAIN. Well, thank you, Mr. Chairman.

Secretary Evans, you did business in the State of Texas before you came here to Washington. What has been the impact of the North American Free Trade Agreement on the economy of your State?

Secretary EVANS. Well, Senator, it has been a very positive impact, as it has been, I think, on the country. I mean, I see we have had a very healthy economy in the State of Texas for the last 6, 7 years since the initiation, since the implementation of NAFTA. I have seen the same thing with respect to the national economy. The national economy obviously has performed very well over the last 7 years. I think that is in part because of NAFTA and the Uruguay Round.

So it has been a very positive impact on the State of Texas on balance and also on the U.S. from what I can see.

Senator MCCAIN. Well, I think another important factor is the effect on the economy of Mexico. We all know that as long as the Mexican economy is dramatically worse than ours, Mexican citizens will continue to try to come to the United States to find work. Yet in my visits, I see that the best and healthiest part of the Mexican economy is in northern Mexico, where the Free Trade Agreement has had its greatest effect.

I would appreciate if you would submit for the record not only the benefits to the U.S. economy, and job-related, because everybody is entitled to their opinion and obviously, we have different opinions on this Committee, but not everybody is entitled to their facts. I think it is important that you would submit to the record the facts, not only as far as the impact on the United States economy, but also the Mexican economy, because we know we continue to have significant problems of illegal immigration, drugs, etcetera.

[The material referred to was not provided to the Committee.]

Have you got, off the top of your head, information concerning the impact on the Mexican economy of the North American Free Trade Agreement?

Secretary EVANS. Senator, I do not have information off the top of my head. I likewise met with Minister Derbez yesterday, and he talked about his economy. We were talking about our economies right now. He said that, he referred to the border states in Mexico and the strength of those border states as a result of NAFTA, and he feels like that those border states are doing well through this slowdown period.

But I will be glad to get you some specific facts and specific numbers as to what it has meant for the Mexico economy.

Senator MCCAIN. You know, one of the interesting things about the recent election in Mexico is that Mr. Fox's strongest support was, guess where? Where the economy was the healthiest, in the

northern part of that country. I took no sides in that election. No American had the right to. But it is interesting that, for the first time in 70 years, there is another government in power in Mexico, and this government clearly has already taken some steps that I think are important, including the extradition of drug dealers to the United States of America for the first time, as well as increased cooperation on the border on drug enforcement and other issues, as well as some very innovative ideas that President Bush and Presidente Fox are sharing in ways that we could relieve our immigration difficulties as well as addressing some of the drug problems.

I thank you, Secretary Evans, for being here. I thank you for your commitment to free trade, which is really what President Bush also campaigned on in his campaign for the presidency. I am glad to see that the President is standing up to what is clearly blatant protectionism, which is on the rise in the Congress of the United States and, unfortunately, to some degree around the country. I thank you, Mr. Secretary.

Thank you, Mr. Chairman.

The CHAIRMAN. Senator Allen.

Senator ALLEN. Thank you, Mr. Chairman.

To follow up on just a comment on what Senator McCain was saying; generally speaking, what I think has been seen is when we do have these trade agreements—obviously, my main concern is what is the impact on Virginia, what is the impact on the people of America. But usually when you have a good trade agreement, the United States exports more than whatever that product or good may be. You are exporting our concepts, our constitutional principles of due process, of private property rights, the rule of law, respect for private property. So that is very, very important, I think, for all human beings. So that is I think our best export of all, and that is our concept of individual liberty and freedom and protection of human rights.

Now, on the issue of compliance that the Chairman brought up: it has come to my attention, I am sure you are no doubt aware, about the serious and rising disparity in market access between the United States and the Korean automobile markets, with the Koreans increasing sales in the United States by double digits annually over the last 3 years, to nearly 700,000 cars projected this year.

Now, I find nothing wrong with that. That is good for our consumers, that they are able to purchase and have the choice and opportunity to purchase these quality automobiles, and I am not saying that we ought to stop those cars from coming in and our consumers from purchasing them if they so desire, competing with cars made in this country or elsewhere in the world, wherever the company is headquartered.

But when they sell 700,000 cars here, all foreign automakers in Korea sold just 4,414 cars last year. Now, that is all. That is not just U.S., that is Japanese, German, French, Italian, and whatever, Czech, everything. So it is an issue of great concern for those who are involved in the automobile industry.

There has been this U.S.-Korea auto agreement in place since 1998. Yet there has been no apparent opening of the Korean domestic auto market to U.S. automakers.

So my question to you is, for me and for everyone, what will you do, along with the Bush Administration, the rest of the Administration charged with overseeing this U.S. trade policy agenda, to ensure that Korea opens their markets to our U.S. autos?

Secretary EVANS. Well, Senator, as you mentioned, we signed an MOU with Korea in 1998 and I think there were four basic parts to it. One of the key elements of the MOU is perception. Korea for many years has had this buy-Korea kind of campaign, and when President Kim was here earlier in the spring I spoke with him about this very issue, that we were concerned that—the numbers I had was that we were importing 426,000 cars from Korea and the U.S. was exporting to Korea 1,200 cars.

I do not understand putting an MOU in place in 1998 with the idea of addressing this wide disparity and looking at it 3 years later and nothing has happened. So that was the point I tried to express to him: what is the purpose of signing agreements and MOUs with principles of how we are going to close the gap and nothing happens.

So all I can tell you is that I guess at the highest level we have expressed our concern, we are going to meet on it again and keep the pressure on and monitor it. You know, back to Senator Hollings' earlier comments about compliance, this was a memorandum of understanding. I realize it does not carry the same weight as a trade agreement. But still, you are agreeing to try and close the gap.

Back to what Senator Hollings was saying earlier about compliance, we have got to, as we move into opening up markets around the world, we have got to make sure the playing field is level and we are all playing by the same rules and these markets are going to be accessible to us. It does not look like to me that the Korean auto market right now is very accessible to American workers.

So I do not know anything that dispirits our workers or our businesses any quicker than to think that there is not a level playing field out there, that we are not playing on a level playing field with the Korean auto workers today. We do not mind competing with them, but the idea that they are shipping 450,000 cars over here and we are shipping 1,200 cars over there, there is something that is not right.

So anyway, all I can say is we will keep the pressure on and we have mentioned it to President Kim and we will follow up on it.

Senator ALLEN. Thank you, Mr. Secretary.

Thank you, Mr. Chairman.

The CHAIRMAN. Thank you.

Senator Nelson.

STATEMENT OF HON. BILL NELSON, U.S. SENATOR FROM FLORIDA

Senator NELSON. Thank you, Mr. Chairman.

Mr. Secretary, I want to help you with your trade agreements. I am basically a free trader. Let me describe to you what happened under NAFTA in Florida, recognizing that not only do we have an obligation to represent the interests of the country in our votes, but we also have an obligation to look out after our own people.

In the passage of NAFTA there were side agreements to protect the winter vegetables in Florida, primarily tomatoes.

Those side agreements were not kept. As a result, whereas 90 percent of the winter vegetables used to come from South Dade County, that is now down to about 35 percent. One-hundred tomato farmers, as a result of that side agreement being broken in Florida, have gone out of business. Twenty-four packinghouses have gone out of business.

Now, since I want to help you, what would be your advice to me as we approach, first of all, this Fast Track, and then later on, additional trade agreements?

Secretary EVANS. Well, again my counsel would be that we want to work with you in enforcing side agreements or trade agreements. If these side agreements are not being enforced and we need to take action, then we are ready to do it. One of the initiatives that we started in the Department of Commerce was a compliance outreach program, and we have asked each Member of Congress to designate somebody in their office that we can communicate with to deal with compliance issues.

What I would say is let us sit down with your team and let us look at this in a very deliberate way, and if people are not in compliance with the agreements then we will take the necessary steps. I am somebody who believes in results, and we see a problem, I want to deal with it.

Specifically, I do not know the depth of the tomato issue right now to respond other than that.

Senator NELSON. That is very helpful and that with regard to trade agreements already made. Now, as we get to looking about trade agreements in the future, give me your ideas about congressional consultations, even to the point of having a congressional trade adviser in overseeing the negotiations, so that we have direct congressional involvement in the negotiation process?

Secretary EVANS. Well, it is certainly about a partnership. It is certainly about trust. It is certainly about working together when it comes to negotiating trade agreements. Exactly what form that takes, whether or not there is a specific committee or a specific individual, I am not sure. But there should not be any confusion at all about the principle of an active dialog and cooperation and a spirit of cooperation between Congress and the Executive Branch when it comes to negotiating trade agreements.

What trade promotion authority should do for us is define the objectives and define the parameters by which you would expect the President to return a trade agreement to this body.

But along the way there needs to be active dialog, and I think we are taking steps that we think are constructive in facilitating that.

Take the Free Trade Area of the Americas. For the first time ever, we have said that needs to be, as we go through the draft and go through the work in progress, it ought to be a public document, it ought to be out there for everybody to look at and review and discuss.

So, I do not know any better way to provide for, to facilitate an active kind of discussion, than to lay it out there as you are going through the negotiation. So I think the Free Trade Area of the

Americas, the first time ever we have said, that I know about—I have been told it is the first time ever—that we are going to take this trade agreement that we are negotiating and let everybody look at it and talk about it, and what are your concerns and what should we be thinking about.

I think that it is a lot about trust, and it is a lot about trust that we will work with you and listen to you and talk you through the process. But the principle of the President having the authority to sit down at the negotiating table, on behalf of the American people, and negotiate an agreement that he would bring back to the Congress for an up or down vote, I understand that principle when it comes to leading on trade.

If America really wants to lead the world on trade, then I think that is authority that the President needs to have.

But never lose sight of the fact of the important role—the good Chairman mentioned it earlier—in the Constitution. I have great respect for what the Constitution says, of course, to the responsibility of Congress when it comes to trade. So there is no question about us understanding this authority and the importance of it and what the Constitution says about it with respect to the Congress.

Again, I think it is a partnership, it is working together. I do not know exactly what the mechanism is or exactly whether or not there is a certain person or a committee or whatever. But the principle of openness and dialog through the negotiations, I think, is important.

Senator NELSON. Well, I certainly embrace partnership and mutual understanding, particularly with regard to our role, as you noted, in the Constitution, of advising before we consent. I respect that you might not want to offer a particular conclusion about Congressional trade advisers in the course of the negotiations. But I wish you would get back to us as to what you conclude, recognizing what you say about the Administration negotiating on its own.

But the fact is that you have got folks like me that want to help you, but we have also got to look out for our people, and we see how we have been burned. An example is the tomato farmers. So perhaps we need to be a part, or a representative, or an adviser as a part of that process, instead of just having a take-it-or-leave-it kind of decision that we would have to make.

Mr. Chairman, I will wait for a second round here. I have got a couple more questions.

The CHAIRMAN. Senator Dorgan.

STATEMENT OF HON. BYRON L. DORGAN, U.S. SENATOR FROM NORTH DAKOTA

Senator DORGAN. Mr. Chairman, thank you very much. I have a markup in the Energy Committee and so I have been delayed and was not here when you opened. I regret that.

Mr. Secretary, thank you for being here. I must say I am a big fan of yours. I was happy to support your nomination, am pleased that you are where you are. But you should know that I will be an aggressive opponent of so-called Fast Track Trade Authority, and I want to take just a moment to explain why, and then I do have some questions if we have time.

I think this country has lacked backbone, will, and nerve in dealing with our trading partners. We have done it consistently. I think I could blindfold myself today and listen to you and I could listen to the Clinton Administration and the Bush Administration and the Reagan Administration and if the voice were distorted I would not know which Administration was speaking.

It is always that everything is working just fine, when, in fact, we are sinking deep into a pit of trade deficits that are growing and growing and growing. I would say to my colleague Senator Nelson, the only way you can reconcile what is happening in Florida relative to the trade agreement, NAFTA, is to ignore the facts. Only then can you say this is a resounding success.

Let me demonstrate why that is the case with some statistics. Let me before I do that, say that I would say to this Administration, as I said to the previous Administration, why do you not, if you are interested in Fast Track, fast track some solutions to the problems created by the recently negotiated trade agreements before you ask that we fast track legislative procedures so that we can do new trade agreements.

Those problems created by previous trade agreements are limited to, but not exclusively, stuffed molasses from Canada, by which Brazilian sugar comes in in the form of molasses as a carrier, and then the sugar is unloaded and it goes right back, the molasses goes back to Canada. So that is the way we slip Brazilian sugar into this country.

Korea: 450,000 to 500,000 Korean cars into this country. We ship 1,200 to 1,400 to Korea.

How about potato flakes? Raise some potatoes in the Red River Valley, flake them and send potato flakes to be used in fast food to Korea. Guess what? They impose a 300 percent tariff on potato flakes, for God's sake.

Japan, 12 years after the last Japanese-U.S. beef agreement, which our negotiators celebrated, there is a 38.5 percent tariff on every single pound of beef going into Japan from the United States. Put a T-bone steak into Tokyo, a 38.5 percent tariff on it, 12 years after the beef agreement.

China—I guess I will not go on, but you get my point.

I could go through 15 or 20 of these. The point is we have recurring dramatic problems, no one lifts a finger to help.

Everyone says, yes, we have got problems, we are going to "monitor." That is what the Clinton Administration said. It is what every Administration says, and nothing ever happens.

The merchandise trade deficit is about a billion-and-a-half dollars, a billion-and-a-third dollars a day, every single day. It is a relentlessly growing trade deficit that weakens this country.

Mr. Secretary, while we disagree on this, I have great respect for you, but NAFTA has been a disaster for this country. We turned a very small surplus with Mexico into a very large deficit. We took a moderate deficit with Canada and much more than doubled it. NAFTA has, in my judgment, been a disaster for our country, because it was also, in my judgment, incompetently negotiated, as have been many of our recent trade agreements.

You have, Mr. Secretary, about seven to nine people monitoring all of our China trade down at the Department of Commerce. You

have, I think, seven people monitoring Japan trade, 13 people monitoring trade with Canada and Mexico. In all of those cases, those are fewer people than you used to have at Commerce, because enforcement has not been something we have been very interested in.

We want to rush off and negotiate a new agreement. That has always been our deal: Go rush off and negotiate a new agreement. Our negotiators have been able to lose in the first week or 2 with every trade round. I just am tired of it. I am not going to support additional Fast Track.

I will say this: Let us agree, this Administration and this Congress, to start fast tracking some solutions, just three or four. Fast track a few solutions to say that we are serious about this, and then let us get together about what kind of trade agreements we want in the future.

Sorry you had to listen to that, but it is important. It is therapeutic for me to say it.

Let me ask the question, if I have any time left: How on earth could not only this Administration, but the previous Administration, which is of my party, how could anyone tell me that our trade agreements are working when the trade agreements are producing trade deficits that are spiking in a very dramatic way. Our current merchandise trade deficit is roughly $450 billion a year, up dramatically. How can that be a sign that the trade agreements are working, Mr. Secretary?

Secretary EVANS. Well, I guess my own perspective is, Senator, I have got great respect for your views, of course. But my view is that I look at the American economy over the past 10 years and we have gone through one of the most robust periods of growth we have in the history of America. When I travel around the world talking to other leaders, they are amazed at the power of our economy to generate and create jobs.

We created some 20 million jobs during the decade of the 1990s. When I look at our overall unemployment in America, I see it down at some of the lowest levels we have seen in over a generation. So when I look at kind of the macro numbers of our economy, I see good signs. Obviously, the economy today is not doing what we would like for it to be doing, but there are some good healthy signs.

Senator DORGAN. Are you concerned about the trade deficit?

Secretary EVANS. I am concerned about the growth of the economy, of the American economy. I am concerned about growing jobs. I think what we do—my view is what we do is try and create the environment, create the framework by which our economy will grow and prosper and will generate, create economic growth, create new jobs, create a higher standard of living.

I think there are a lot of parts to that. I think monetary policy, I think fiscal policy, I think trade policy, regulations and rules that we pass is a part of the framework that is an environment for this economy, are all part of what shapes the American economy.

So I am concerned that we have a friendly kind of environment for this economy to continue to grow. So when I see gross domestic product growing at over 3 percent throughout the 1990s; when I see unemployment rates down at—it got down to 3.9; I guess it is 4.5 now—and I look at other economies around the world, I feel

like our economy, over the last 10 years or so, is certainly one to be proud of.

Senator DORGAN. Mr. Chairman, I know that my colleagues want to ask additional questions. I do as well.

The CHAIRMAN. We will come back.

Senator DORGAN. I do want to further plumb the issue.

The CHAIRMAN. Absolutely.

Senator NELSON. Mr. Chairman, before the gentleman from North Dakota leaves, I just want to say he raised as an example of abrogation of trade agreements bringing sugar through Canada in the form of some hardened state that then is reconstituted in America. Now, that is not what the trade agreement is supposed to be, and yet it is being done.

So what we would like is we would like you in the Executive Branch of government to stop it. If we have to supply you with some additional tools in law, then we clearly want to do it. But it is an example. It came close to home, because there is a lot of sugar in Florida. And what is the agreement on trade with regard to sugar, which affects his constituency as well, is being broken.

We would like to see some resolve so that it would stop being broken and stop adding to the thickness of that big red book over there.

The CHAIRMAN. Mr. Secretary, do you want to comment, or let me comment?

Secretary EVANS. I want to hear.

The CHAIRMAN. What happens is you heard my colleague to the right about protectionism. Free trade, everybody is for free trade. It is like world peace, it is how you get it. That is what we are talking about.

Jobs are not just jobs, creating jobs. It is creating manufacturing jobs. Let me go to Akeo Morita. It was almost 20 years ago in a seminar in Chicago, lecturing these emerging nations, and he said the Third World emerging countries could not become really a nation-state unless they created a strong manufacturing capacity. And he said, and Senator, because I was there, later on he said: “And by the way, that nation that loses its manufacturing capacity, that world power, will cease to be a world power.”

Now, after World War II, we had 41 percent of our work force in manufacturing. By 1965, we had 29 percent. I have just checked and now we have got 12 percent. Yes, jobs.

Barbara Einrich, “Nickel and Dime,” she talked about the jobs.

They are all cleaning up, tourism jobs, making beds, flipping hamburgers and everything else like that. But the strong manufacturing jobs, those jobs that create the middle class, that give strength to the democracy—our security, like a three-legged stool, we have got the one leg of our values as a Nation admired the world over with respect to individual rights, democracy, human rights.

The second leg, military, is unquestioned. But the third leg, economic, has been fractured as a result of the struggle in the Cold War. Now, we predominated, we won. We passed the Marshall Plan. We gave up—I will never forget, when I told you earlier, I testified 40 years ago. Governor Dewey said to me: “What do you

expect them to make? Let them make the shoes and the clothing and we will make the airplanes and computers."

Well, I am looking here and over two-thirds, around 70 percent of the clothing I am looking at is imported. 86 percent of the shoes on the floor are imported. They are making not only the shoes and the clothing, but the airplanes and computers.

That gets me back to your statement. This is what you stated just a couple of weeks ago here before the Finance Committee: "In other words, free trade lets us focus on what we do best."

What do we do best?

Secretary EVANS. Compete.

The CHAIRMAN. How? How do we compete when we are losing all these manufacturing jobs? I mean, what do we make best? What do we create best that someone else does not?

Secretary EVANS. Well, Senator, I think that the economy is saying that we are creating a lot of things best. Again, when you look at the growth of our economy and you look at the jobs we are creating, these export jobs pay some 13 percent to 18 percent more than the national average. But I think there is a wide variety of products that we make best, obviously in the whole high tech sector, I would say in the textile sector.

The CHAIRMAN. Textiles?

Secretary EVANS. Well, textile exports have been trending upwards over the last 4 or 5 years, the last data that I looked at.

The CHAIRMAN. Mr. Secretary, right to the point, we do not really produce anything best any more. You can transfer the technology by computer, you can transfer the financing by way of the satellite. You can start up and run your plant from Austin, Texas, in downtown Bangalore, India, and they are doing it; or Dublin, Ireland, or anywhere else down in Mexico, and with the wage scale and everything else.

My point is we are the trustees of the economy, and the economy is not strong. We had to borrow $51 billion yesterday in order to mail out rebates. Come on. The economy is not strong. I am losing out here and I am being told I am winning.

The truth of the matter is we did win. I want to give you some hope in my little bit of time. Ronald Reagan was good. I wanted Zellick to come on up here, because he worked for our friend Jim Baker, and it was in his time over there in the White House. Ronald Reagan was good; he saved Andy Grove and Intel. He put in Sematech. Right here, Senator Danforth and I, we put in Sematech and a voluntary restraint agreement on semiconductors.

Now we have a deficit in the balance of trade in semiconductors, because of the very thing I just described: Intel has built the best and the newest plant for semiconductors in Dublin, Ireland, using, incidentally, my technical training program. Ask Frank McCabe; he runs the plant. I have been there.

But I can tell you here and now that we are into a competition worldwide. The competition is market forces, it is not free trade. We are not using our big, fat, rich American market in order to really get these deals. We are going to have to really raise a barrier in order to remove a barrier.

President Reagan put it in, voluntary restraint agreements on steel, machine tools, semiconductors, and one other thing, and I see

you folks are moving on steel. Move faster, because I have got steel plants. You see, the World Bank goes around over there and they run to every little nation-state and say: "You have got to produce the tools of agriculture and the weapons of war," and they give them a 2 percent steel plant. We have got a glut of steel plants the world around, and I am importing right over my docks in Charleston, Brazilian steel, and I have got the most efficient, Nucor. There is not any question of productivity. I have got the most efficient steel plants you can find in the world.

But that is the kind of thing that the Executive Branch—and I liked Senator Dorgan's comment with respect to the last Administration. We worked on them. It is not partisan.

We love you. We think you are the best Secretary of Commerce we have had in a long time. But just do not go down the road saying everything is fine and we have got a strong economy and we have got the division over there for compliance, because it ain't working. I can tell you that. We are going out of business.

Let me yield and let you comment.

Secretary EVANS. Well, look, back to the point on compliance. You mentioned our 201 initiative by the President. I do not think there is anything more important than sending the strong message out there that we are all going to play by the rules and there is going to be a level playing field. I have seen the additional resources that have been added to compliance. It is something that we are going to continue to stay focused on.

If others are breaking the rules, then there need to be consequences. On molasses, if rules are being broken, if laws are being broken, there need to be consequences. I am not confused about that at all. So you just have my commitment and assurance from me that you bring to us situations where you can show that people are violating the law, violating the rules, I am going to do what I can to deliver and make sure that they are held in compliance and there are consequences for that.

The CHAIRMAN. Very good. When we saw we are going to lead the world on trade, what we are doing, unfortunately, is leading the world on trade deficits.

I mentioned Hamilton and Jefferson a little while ago, because the very second Act that passed the national Congress in history—the first one was for the seal, but on July 4th, 1789—was protectionism, a tariff bill of 50 percent on 60 articles, because Jefferson was looking out for the farmers and old Alexander Hamilton was looking out for production.

David Ricardo came with this same thing about what we do best. He said the doctrine of comparative advantage, he said to the little fledgling colony: "Now that you have got your freedom, we will trade with you what we do best and you trade with us back what you do best."

Old Hamilton, "Report on Manufacturers"—here it is. I had to get that from the Library of Congress. The Library of Congress has got the only original copy left. But in his "Report on Manufacturers," Alexander Hamilton said: "Bug off; we are not going to remain your colony, just shipping you the iron ore and the timber and the cotton, rice, and indigo, the agricultural products, and bringing in

the manufacturers. We are going to develop our own manufacturing capacity and strength."

That is why they passed that tariff bill, which Madison finally agreed to and joined in and helped it get passed.

So you have got to protect the economy. You have got to build. You have got to have that wonderful economy. You are a good businessman, you are a builder, and let us get to building and really enforce these agreements, like you have attested to.

Senator Dorgan.

Senator DORGAN. Mr. Chairman, thank you.

I wonder whether perhaps in the years ahead at some point we will scratch our heads and wonder to ourselves why we did not understand that you cannot run a $450 billion merchandise trade deficit without there being consequences. People felt 2 years ago the NASDAQ was always going to keep going up and now they are scratching their heads and wondering, "Why did we not understand you cannot buy stocks at 150 times price-earnings?"

I think that the growing trade deficit is of great concern, and the fact that we have a growing economy as the trade deficit grows ought not be a case to ignore the trade deficit. I know a lot of smokers that are having a pretty good time as well, but they will have consequences in some cases. So it seems to me—I was trying to ask you, do you think the growing trade deficit is a cause for alarm or a cause for concern? Should there in this country be a designed attempt to address the burgeoning trade deficit?

Secretary EVANS. Well, I think the trade deficit is something that we should pay attention to. Senator, we import about 60 to 65 percent of the crude oil that we consume in this country today. That is a substantial part of the growing trade deficit. I do not see any change in that trend in the years ahead.

The trade deficit as we have watched it over the last several months has been coming back down. It has been drifting down from the high of $435 million, whatever the number was——

Senator DORGAN. Billion.

Secretary EVANS. Billion I mean, over the last—in 2000.

I think it is also instructive to point to the fact that, in terms of net foreign direct investment, it was $269 billion more invested here in America from foreign countries than we invested outside the United States. So that is, I think, another part of this economy.

But to say that we ought to make any dramatic changes to bring the trade deficit down, I cannot see that. As long as our economy, we continue to see—again, it is monetary policy, it is fiscal policy, it is rules and regulations, it is creating the framework for this economy to continue to grow, which I feel like it has been at a pretty healthy clip over the last 10 years.

Senator DORGAN. Mr. Secretary, I wish I had received an answer that is more comforting. I wish you had said "yes." I think this is alarming, I think we have a circumstance where we have trade deficits that have grown in a way that is not healthy for this economy, it increases the current account deficits.

The result of foreign investment is a natural result, in my judgment, in running the current account deficit and the foreign trade deficit.

But, having said all of that, let me ask you a question.

You talked about consequences. Will there be consequences, for example, for Canada, who has a Canadian Wheat Board which is a state trading enterprise, a monopoly that would be illegal in this country, that thumbs its nose at you, at the USTR, at the GAO, and at all attempts to get information about the price at which they are selling their wheat into this country? We allege that they are dumping into this country, they are selling below acquisition cost, violating trade agreements, and they retain exclusively all of the information by which you could make that case. When the U.S. Government requests the information, they say: Take a hike.

Will there be consequences for a country that does that with respect to the durum wheat trade?

Secretary EVANS. Well, Senator, I sure think they ought to share the information with us. I have not looked at it specifically, but I will. I think we have a good working relationship with Canada. We are dealing with them on a number of issues, softwood lumber, as you know. We took some aggressive steps on that issue that I think sent a signal that said, look, we are going to monitor and we are going to watch and people are going to comply with these laws. We set up a monitoring system at the border that allowed us to monitor softwood lumber on a daily basis.

So we have got a good working relationship with them. I do not know why that would change.

Senator DORGAN. Well, we do not have a good working relationship. We have been monitoring this for 8 years and the Clinton Administration monitored it, the George W. Bush Administration monitored it, and through all of this monitoring, Canada has gone right ahead and continued this terribly unfair trade that has cut the ground out from under our farmers.

Mr. Secretary, I think I mentioned to you when you were out for the nomination hearing, I went to the border in a 12-year-old orange truck with Earl Jensen with a couple of hundred bushels of durum wheat. All the way to the border, the Canadian trucks were coming south with 18-wheel trucks hauling Canadian durum. But Earl and I could not get a 12-year-old orange truck through the border, because that border was closed to American durum even as they were unfairly putting their durum into our marketplace.

My point is we have monitored this forever. Nobody has ever really done anything. Our farmers are still victims. My only question is, if the Canadian Wheat Board, which is a monopoly that would be illegal here, continues to thumb its nose at this country and say, “We will not allow you access to information about how we are selling into this country”, will there be consequences? There have not been for the last 10 years.

I hope you will tell me, yes, there will be consequences; I intend to see to it.

Secretary EVANS. Sure. I will get back to you. You bet, Senator.

Senator DORGAN. Let me go back to Korea, because I think the question is an important one. If a country like Korea is shipping us a half-a-million cars a year, and buys 1,200 or 1,400 cars from us—why? Well, a fully equipped Ford Mustang would cost $55,000 in Korea. Sound unreasonable? Does to me.

So if that continues, and in 1998 they said, “Oh, we will be better, we will do better.” It is 2001, and nothing is happening, what are the consequences for Korea?

Secretary EVANS. I am not sure, Senator, but I made the same point earlier. We signed an agreement 3 years ago. It does not look like to me much has happened. What was the agreement all about? What was the memorandum of understanding about?

Senator DORGAN. My point is, nobody ever does anything.

We lack nerve, will, and backbone to stand up to trading partners and say: “Look, our market is open to you, God bless you; our consumers are advantaged by having access to the broadest array of products; but understand us, if we are going to do that then your market must be open to us.”

You know how many U.S. movies got into China last year? Twelve. Now, some might argue that is an advantage for China. But my point is, all across the board, we are being shortchanged, because this country lacks will. All we do is chant, like these street corner chants: “Free trade, free trade.”

The fact is, all I care about is expanding opportunities for trade in a manner that is fair to American producers.

When we get to that point, I am going to be the one that applauds and says: “I am on your team; let us go together and do this.” But until that time, I want to see some evidence of fast tracking solutions to the problems that have been created the last 6 or 8 years. I see no evidence in the previous Administration and I want to see some from you. But until that time, I do not support Fast Track.

Secretary EVANS. The only evidence that I can point to right now is 201 on steel. I do not know anybody else before us that wanted to step up and initiate a 201 on steel, and we did. I want to look for other opportunities to send a signal to the world that if you are going to trade with the United States of America, you are going to comply with the agreements, and your markets are going to be open to us, and there is going to be a level playing field and you are going to play by the rules. I welcome more opportunities like steel and initiating a 201 to send that message.

Senator DORGAN. Well, I tell you what. Potato flakes to Korea, T-bone steaks to Tokyo, durum wheat from Canada. I will give you a dozen or so. Sink your teeth into them, and I am going to be on your team.

But until I see all of that, I will say to you, as I did to the Clinton Administration, I think that trade agreements that have the capacity to increase our trade deficit are not in our interest. But if we can work together to solve problems created by the most recent trade agreements, I want to do that.

Let me finish where I started. I am glad that you were nominated by President Bush. I think you have the capacity to do a lot of good things. While we might disagree on Fast Track, and we will disagree aggressively on that, I want to work with you on a range of things.

This Congress has the responsibility to put money—and I am working on that—in your accounts on trade compliance with China, Japan, Europe and Canada and Mexico.

We need to not just "monitor" in the ethereal way. We need real people monitoring those every day, so that we understand what is happening in our trade relationships.

Secretary EVANS. Thank you, Senator.

The CHAIRMAN. Mr. Secretary, we really do appreciate and admire your leadership with respect to the 201 steel case you raised. We have been trying and trying and trying, and we could not get it before the previous Administration, and we commend this Administration for its leadership on that score.

One final thing, because we have got a very important panel that follows you, is that you should understand that as the Secretary that your best friends are against you on what you were attesting to, namely that you were going to enforce compliance. The truth of the matter is, when I first came up here years back, it was the Japanese representative in the office, it was the Korean representative. They do not even bother to come, their lawyers. The big business, the multinationals—the "non-nationals," I call them—are leading the way.

There is no more admired individual in the business field than Jack Welch of GE. Just a year-and-a-half ago, this is a *BusinessWeek* article. He said that they were not going to have any subcontractor that did not move to Mexico, and they talked about having 30,000 already there. GE even puts on supplier migration conferences to help them make the leap.

Now, what happens is we are exporting the jobs. We are not exporting the products. Trade is not for investment. I do not see why I should encourage the investment in China or the investment in Mexico. I would love to have the investment in the United States, but my duty is to try to create the jobs.

What happens here is after we passed PNTR with China, *The Wall Street Journal* headlined it, it was nothing but an investment program and policy. Go right to Doha and Qatar.

Later here, in November, I think, is the conference. They holler free trade because they like to dump, and they come in and the dumping violation and everything else like that are not enforced now.

I wish we had your Trade Administration. That is why I say let us abolish the International Trade Commission, because we find the violation at the level of the Trade Administration in the Department of Commerce, but then we go over to that crowd in the International Trade Commission and they never find any real injury. So the electronics business is gone, and you can go right on down the list: Kodak, hand tools, everything else like that. The lawyers just said "Forget it, no use to take the case to Washington, because they are going to find against you anyway," and you have even got them leading now. The National Chamber of Commerce is not interested in the Main Street merchant in Austin, Texas. He is interested in the multinationals, the internationals.

They are working, like you say, they have got to report to their shareholders. So I cannot fault them for that. They are making more money. But we are the trustees up here of the strength of the economy. You are, I am. It is dwindling every day. We are going out of business. We do have this tremendous deficit. We are transferring into the haves and the have-nots. The take-home pay of the

industrial worker is less than what it was in 1979. So with all the new jobs and everything, $6 and $7 an hour, as Barbara Enrich has described, they cannot find a place to stay, they cannot keep up their health bills or anything else of that kind, and the solution is high tech, high tech.

Silicon Valley, 42 percent of them on part time, no health care, no retirement benefits and everything else, and they do not create the number of jobs. You know, Bill Gates has got 20,000, but Boeing has got 90,000. I mean, the real jobs are in manufacturing, and in the oil business and certainly not in the blooming high tech business. They have fired them all.

So we really appreciate it. Let me yield for your comment and anything else Senator Dorgan wants to say. But we have got a roll call here now on the floor.

Secretary EVANS. Senator, I just would say what I did earlier: I think this is the time America has got to make the decision that we are going to lead on trade. As I look at the world economy and consider that in 1970, 10 percent of the GDP in the world was trade, and today about 25 percent of it is trade, there is not any question in my mind that we are going to continue to increase trade in the world.

When I think about the fact we have got 400 million people connected to the Internet today and over the next 4 or 5 years that will increase to 1 billion people connected to the Internet and 90 percent of those additional people will be outside the United States, it tells me that this world is going to continue to open up markets. I just think that our economy needs the certainty, needs the commitment that America is going to lead that effort.

The way for us to send that signal to our economy, our financial markets, our capital markets, our business community, is to grant the President trade promotion authority. So I am going to, obviously, continue to be up here, continue to work on that, work with you, listen to you.

I appreciate your comments this morning. I got the compliance message loud and clear. I am not confused about that.

I have been in office for 6 months. I know it is a big concern here. I want to see every opportunity that I can find to deliver a strong message that if you trade with America, if you sign agreements with America, that you are going to comply, and if you do not there are going to be consequences.

That is exactly why I called Attorney General Ashcroft on this whole trans-shipment area. It bothers me that Customs catches people and then they get into the Justice system and nothing ever happens.

So when I talked to him, he assigned a task force in the Justice Department to look at that and see if that indeed is what is going on. Are those cases backing up? And if they are backing up, how come? What are we going to do about it? What additional resources do we need to put on those cases to make sure that there are consequences?

So will it take more resources to enforce these agreements? It might. I know Senator Dorgan mentioned, and I know, Senator, you had a big role in adding the resources to our Department to

increase the manpower. We are adding 65 people. We need to continue that.

So I take away from this hearing this morning the strong message about compliance and how important it is and that we have not held people accountable in the past and we must. So I look forward to working with you in that specific area.

Senator Dorgan, I look forward to working with you and your staff on specific issues. If we can find more that we can send a signal, I am ready to send a signal. So far, I think we found one big one, and that is steel. We finally have got an Administration now that is not going to continue to tolerate this subsidization that is going on around the world.

So anyway, I am delighted to be here. Thanks for the message. I got it loud and clear on the compliance.

The CHAIRMAN. The Committee is really indebted. We are very appreciative of your appearance here and your approach to this problem very much.

Secretary EVANS. Thank you.

The CHAIRMAN. Thank you a lot.

The Committee will be at ease.

We will have the next panel: Dr. Edward Luttwak of the Center for Strategic and International Studies; Bill Reinsch of the National Foreign Trade Council; and Dr. Alan Tonelson, a Research Fellow at the United States Business and Industry Council.

We have got a vote.

[Recess from 11:13 a.m. to 11:30 a.m.]

The CHAIRMAN. The hearing will come back to order. My apologies to this distinguished panel. This does not do you justice. We are going to have to have you back. The truth is, we are trying to end up 2 months work in 2 days here before we get out this weekend for the August break. It is like Senator Dorgan and others, he has got another markup. I am supposed to be at three more. But this is the most important one.

Let me begin over here with Mr. Tonelson. The full statements will all be included in the record. You summarize as you wish.

STATEMENT OF ALAN TONELSON, RESEARCH FELLOW, UNITED STATES BUSINESS AND INDUSTRY COUNCIL EDUCATIONAL FOUNDATION

Mr. TONELSON. Thank you very much, Mr. Chairman. Good morning. As you said, my name is Alan Tonelson. My organization, the United States Business and Industrial Council Educational Foundation, and I are greatly honored by your invitation to testify this morning. We represent largely small and medium-sized manufacturing companies, who are strongly concerned about the future of a highly diversified American manufacturing base and the American working class.

The announcement by the House leadership yesterday that the vote on Fast Track trade promotion authority will be postponed is only the latest sign that the kinds of trade agreements negotiated by presidents of both parties recently are deeply unpopular with the American people. Poll after poll over the past 6 or 7 years underscores the widespread view that these agreements have not lived up to their promises.

Surely a principal reason is that these very trade agreements generally have been sold under false pretenses.

Americans and their representatives have been told these are trade agreements. In fact, they are more accurately described as investment agreements and there is a big difference. This point, I think, is very important to underscore, that the purpose of our investigation here today is not to judge whether the U.S. economy as a whole is strong or weak, not to judge whether the U.S. economy as a whole is on a truly sound and solid basis or an unsustainable basis. The purpose of our investigation today is to figure out what role trade and globalization policies are playing in that American economy, and in particular, are they contributing to the strength of that economy or are they posing more problems than they are actually solving? So I hope we can keep our focus on the role that trade and globalization policies have actually played in recent years.

These recent trade agreements have been sold consistently as agreements designed to boost U.S. net exports and therefore the net demand for U.S. products and workers and the value of those workers. But investment-oriented agreements get much more complicated, and when they are negotiated without addressing some of the major longstanding features of the world economy, these agreements inevitably have the net effect of draining the United States of productive capacity.

These features include all manner of foreign government policies to channel investment into their own economic systems, regardless of market forces, as well as the formal and informal trade barriers and pro-producer, anti-consumer oriented national economic strategies that they have adopted that completely warp international trade flows.

Many of the investment-oriented trade agreements negotiated recently have had a more sophisticated rationale to be sure. They were designed to improve American global competitiveness by farming out relatively unsophisticated manufacturing work abroad to countries like Mexico, freeing up U.S. workers ostensibly to do the higher value work and enabling U.S. companies to dramatically cut costs.

We need to keep in mind that competitiveness entails not only better American corporate performance, but rising living standards for the vast majority of the American work force.

The unprecedented deficits that the United States has piled up in recent decades and the fall in real wages experienced by most Americans for the same 30-year period—and we have to remember these trade policies did not start with NAFTA. This is a longstanding problem. These results show that on an economy-wide net basis even this more sophisticated strategy has failed.

The principal evidence for the investment orientation of U.S. trade agreements falls into two major categories. First, look at the major objects of U.S. trade policy, especially since the mid- or late—well, since the early 1990s:

Mexico, China, Vietnam, sub-Saharan Africa, the Caribbean Basin region, Latin America, Jordan—all countries and regions with almost no sustainable consumer purchasing power whatever,

and all determined and often forced to grow by becoming net exporters.

No U.S. trade policy determined to increase U.S. net exports could possibly focus on countries like these. To turn Willy Sutton's famous comment on its head, in U.S. trade policy "we are going where the money ain't."

Second, as is the case globally, U.S. investment flows abroad have been growing much faster than U.S. exports and our trade deficits make clear how much of this investment has gone into building up export bases overseas, especially in emerging market countries like Mexico and also China. In fact, the study that I put out last year, which I have right here, makes quite clear that when U.S. multinational companies discuss their business plans regarding China, they ignore exports almost completely and emphasize investing and manufacturing in China instead. Exports are almost off the screen for most of the large U.S. companies engaged economically there.

Now, U.S. trade policy has stealthily taken on an investment orientation, but U.S. Government projections of the economic impact of trade agreements have generally ignored this very important trend. Consequently, they have broadly missed the mark in their projections. Too often in trade negotiations, as a result, U.S. negotiators have been flying blind or they have not been telling the American people what they are really up to.

I would like to supplement my written testimony with one brief final point. We desperately—and I underscore that, desperately—need more and better U.S. Government data on U.S. investment flows and their effect on U.S. trade flows.

The Department of Commerce has given us a relatively good start, but its data fails to capture many of the increasingly important ways in which U.S. multinational companies have sent production abroad and other critical developments on the foreign investment front.

By contrast, U.S. multinationals know exactly what they are doing in this regard. They know exactly how their sourcing patterns have changed over time. If they did not, they could not be successful. This is fundamental information for them. But for obvious reasons, they are not talking.

I would be very happy to elaborate on this last point or answer any other questions that you may have, and thank you very much again for the opportunity.

[The prepared statement of Mr. Tonelson follows:]

PREPARED STATEMENT OF ALAN TONELSON, RESEARCH FELLOW,
UNITED STATES BUSINESS AND INDUSTRY COUNCIL EDUCATIONAL FOUNDATION

Good morning. My name is Alan Tonelson. I am a Research Fellow at the United States Business and Industry Council Educational Foundation. I am honored by the opportunity to appear before you today, as is my organization.

The Foundation is the research arm of the U.S. Business and Industry Council, a very distinctive national business organization, at least when it comes to trade and globalization issues. Our companies are predominantly small and medium-sized manufacturers. They believe that the strongest and broadest possible American industrial base employing large and growing numbers of our countrymen is essential for national security, for sustainable prosperity, and for our nation's political and social health. These views explain much of our opposition to the trade liberalization strategies pursued by the United States in recent decades.

In fact, many of the problems created by these policies are conveniently summarized by the premise of these hearings—that most recent U.S. trade agreements are more accurately described as investment agreements. Unfortunately, in our view, the investments generated by these agreements have had the unavoidable impact of displacing many more high paying U.S. jobs, particularly in manufacturing, than they have created.

Unless policymakers and citizens understand the differences between these investment agreements and conventional trade liberalization agreements, they will never be able understand the true impact on the U.S. economy of the current version of globalization, much less change course if they feel the need.

I. TRADE AND INVESTMENT AGREEMENTS ARE DIFFERENT

The flurry of U.S. trade agreements negotiated during the 1990s has generally been presented to Congress and the public as net creators of American jobs and growth, and boosters of wages for American workers. The key supposedly was their capacity to increase exports. The stated logic behind these agreements was compelling. The United States was the world's most open market, and its producers were denied crucial export opportunities by foreign trade barriers. Therefore, any trade agreement that reduced these barriers bilaterally or regionally or globally would bring the greatest benefits to American producers, since most of the market-opening would need to take place abroad.

American leaders further explained that more exports would increase the demand for American products, and thus for American workers. In the process, this increased trade would raise the output of the former and the value of the latter. In addition, recent administrations have contended that export jobs pay considerably better than other comparable jobs, which made increasing exports that much more important.

The rationale for investment agreements inevitably is quite different. If mainstream economic and trade theory are any guide, lowering worldwide barriers to investment makes no sense if economic policy is determined to secure disproportionate benefits for Americans. Liberalization of capital flows means that investors are free to roam the world in search of the highest returns, and to change direction as soon as business conditions change. The prime goal is maximizing global efficiency and growth, which clearly should benefit the United States in most instances, but which may well benefit other countries more. The distribution of gains depends heavily on the world economy's main features and on how investors expect those features to evolve. These characteristics of the world economy, it must be noted, inevitably include the wide variety of interventionist foreign government policies aimed at gaining technology and wealth, and promoting job creation. In short, there would be no guarantees for U.S. domestic producers—workers and companies alike—from the results of indiscriminate investment liberalization.

To their credit, the last two administrations have made efforts to take these complexities into account, and they produced a more sophisticated, more explicitly self-interested justification for the investment features of trade agreements that were becoming increasingly prominent and obvious. Agreements such as NAFTA, they argued, would indeed shift some U.S. production abroad. The net effect, however, would still benefit American companies and workers alike. For the work moved overseas would be relatively unsophisticated and labor-intensive—the low end of ever more complex manufacturing processes that are more economically performed by low-income workers in low-income countries. Not only would the total cost of U.S.-brand products be reduced, resulting in a gain for their global competitiveness. But U.S. workers would be freed up to concentrate on the more lucrative, more capital-intensive phases of manufacturing, which would make better use of their higher skill and education levels.

These arguments were especially compelling in the early 1990s, when U.S. companies and their workers were operating at distinct disadvantages vis-a-vis their European and Japanese competitors in particular. The latter typically exported from protected home markets. As any sports fan knows, winning is always easier when you only need to play offense. Because the U.S. market was so open, however, U.S. firms had to play defense as well. Facilitating the transfer of low-end U.S. manufacturing to low-income countries theoretically could help American business overcome these inequities.

Recent administrations have also taken note of changes in manufacturing techniques and markets that seem to argue for encouraging investment abroad. The emergence of truly global markets for many products means that one-size-fits-all production often will no longer do. Customization to fit local tastes is often necessary, and manufacturing close to or in local markets can help companies keep up

with or ahead of local preferences, and better serve those customers. Dispersed international manufacturing can also help companies cope better with the problems created by fluctuating exchange rates. And finally, since the global distribution of worker and management skills is rarely uniform, some countries and workforces are simply better at developing or making certain products than are others. Washington quite rightly has felt that U.S. business should be free to take advantage of foreign talent and technology.

II. WHEN THEORY FALLS SHORT OF PRACTICE

Unfortunately, the shift from conventional export-oriented trade agreements to investment-oriented agreements has produced at least two major problems. First, this shift was never adequately explained to Congress or the public. In fact, throughout the 1990s, trade agreements were touted overwhelmingly for their export-creating potential. Second, the spread of U.S.-owned manufacturing abroad has not lived up to its promises in terms of promoting net exports and therefore domestic job creation and wages increases, much less economic growth.

Indeed, quite the opposite seems to have occurred. Despite its beneficial potential for the U.S. economy in theory, in practice, the U.S. manufacturing investment that has been channeled abroad by recent trade agreements has almost certainly strengthened foreign manufacturing capabilities at the expense of domestic. In the case of developing countries, this investment has fostered export bases that have served mainly the existing U.S. market, not new foreign customers. Yet even when such offshore production serves local or third country markets, it often displaces U.S. exports, as does much offshore U.S.-owned production in the developed world.

As many supporters of current trade policies observe, the 1990s have seen an enormous flow of direct investment into the United States as well—a development that would seem to obviate concerns that America might be faced with an "investment gap." Three points need to be made in response. First, the overwhelming share of such direct investment consists of merger and acquisition activities—i.e., foreign takeovers of existing U.S. facilities. Some of this investment undoubtedly saves U.S. factories and other facilities that would have gone out of business, but it is highly improbable that most foreign direct investment into the country represents a hunt for distressed assets—as opposed to highly attractive and profitable enterprises. Therefore, such investment is not in any meaningful way adding to America's productive capabilities. Ownership is simply changing hands. Second, there is no reason to think that the new investment-oriented trade treaties—as opposed to the underlying strength of the U.S. economy itself—were significantly responsible for the new investment flows. Finally, supporters of these trade agreements never claimed that new flows into the United States would result from these policies.

In addition, the foreign manufacturing activities of U.S. corporations have hardly been restricted to labor-intensive, low-technology products. Low-income countries like Mexico and China have become major sources of high-tech products for the United States. Indeed, emerging markets run large and growing surpluses with the United States in many high-tech industries.

The results have been import levels that have swamped exports; U.S. trade deficits that are not only widening rapidly, but increasingly concentrated in high-value industries; lost market share for domestic producers; and downward wage pressure on U.S. workers even in advanced industries. Undoubtedly, some individual domestic production sites and workers have gained. But the trade deficits clearly show that, when all the complex economic effects of multinational production chains and their attendant trade flows are netted out, the domestic economy as a whole is a big loser.

At the same time, many U.S. multinational companies have clearly benefited, often maintaining or increasing domestic or global market share, cutting costs, and widening margins. But these benefits do not necessarily accrue to the U.S. production base. That is to say, what has been good for General Motors and others is no longer automatically good for the United States. Indeed, there is precious little evidence that investment-oriented trade agreements have enhanced American competitiveness, if we accept the Packard Commission's definition of this term—the ability to produce goods that succeed in global markets while boosting the living standards of the American workforce.

III. EVIDENCE FOR INVESTMENT ORIENTATION

Two of the clearest signs that investment considerations have dominated recent U.S. trade policy are this policy's tight focus on low-income countries, where only the most modest traditional export markets can be presumed to exist; and the gulf that has opened between U.S. outward-bound investment and U.S. export flows.

A. Targeting the Third World

Perhaps the most striking characteristic of U.S. trade policy during the 1990s has been its preoccupation with the developing world. Save for the Uruguay Round negotiations that led to the creation of the World Trade Organization, and weak, sporadic efforts to open Japanese markets in specific product areas, recent U.S. trade policy has been a Third World trade policy. Its major initiatives have consisted of extending NAFTA to Mexico and Latin America, normalizing trade with China, and liberalizing trade with the Caribbean Basin region, sub-Saharan Africa, and Vietnam. Further, the Bush administration would like the next round of global trade talks to emphasize Third World needs.

Even the Uruguay Round accords, moreover, are notable for their investment-related provisions and implications. In particular, by weakening U.S. trade laws, the agreement created powerful incentives for U.S. companies to serve the U.S. market from abroad. For the prospect of the United States responding effectively to predatory foreign trade practices and restricting access to its markets under any circumstances has been greatly reduced.

The presumed logic behind the Third World focus is expressed in the oft-made observation that 96 percent of the world's population lives outside America's borders, and that most of this population is found in developing countries. Thus Americans, who comprise only 4 percent of humanity, cannot possibly remain prosperous without selling to these countries' consumers. As is just as often observed, many major Third World countries are undergoing transitions from highly interventionist and even outright communist economies to more liberal systems, which allegedly promises to liberate enormous tides of productivity and generate vast amounts of wealth.

Yet this reasoning ignores the main features of Third World populations and workforces—the almost unimaginably low bases they start from, and the demographic forces likely to keep wages, and therefore sustainable purchasing power, near rock bottom.

Developing countries may represent a large and rapidly growing share of the world's population, but they represent a much smaller share of world wealth. America's relatively puny population, for example, all by itself generates some one-third of global output. The European Union and Japan account for big chunks of the rest. Yet U.S. trade policy has backed off from efforts to open Japanese markets, and has conspicuously neglected this mission regarding Europe. Moreover, the huge projected growth of Third World populations is likely to keep wages in these countries abysmally low for the foreseeable future. This population explosion has, in fact, created a worldwide worker glut, which shows up most dramatically in the towering rates of unemployment recorded in Asia, Africa, and Latin America. In pre-crisis Indonesia, for example, the U.S. Embassy in Jakarta pegged the real un- and underemployment rate at 40 percent. In China, economists feel comfortable openly telling Western reporters that urban jobless rates are nearing 20 percent.

Nor should these figures be surprising. When the supply of any product or economic input outstrips demand, the price will fall, all else being equal. And indeed, additional proof of a buyers' market in Third World labor comes from wage figures in these countries. From China to Indonesia to Mexico, inflation-adjusted wages in most of the developing world were falling for much of the 1990s. And where they were rising, e.g., in Korea, they helped created enormous and nearly fatal competitive disadvantages, as demonstrated by the financial crisis that engulfed so many of these countries starting in 1997.

From the standpoint of promoting U.S. exports, the absurd extreme of U.S. trade policy came in the late 1990s, when the Clinton administration began pushing hard for trade liberalization agreements with sub-Saharan Africa, the Caribbean Basin countries, and Vietnam. Yet when President Clinton began touting the need for a sub-Saharan Africa deal, only four of the region's 35 potentially eligible countries had per capita incomes of greater than $800. Fifteen had per capita incomes of less than $300.

Former U.S. Trade Representative Charlene Barshefsky depicted Vietnam in 1999 as a country with "the potential to develop into a rapidly growing economy with significant demand for our products." What she did not mention was that, when she made this claim, Vietnam had only enough hard currency in its treasury to pay for 9 weeks of imports from anywhere.

The picture has been just as mysterious for larger, ostensibly more promising economies like Mexico and China. During his landmark debate with Ross Perot over NAFTA in 1993, Vice President Gore gushed over the Mexican consumers' allegedly voracious hunger for American-made products. But at the time, Mexico's economy was only 3 percent as large as the U.S. economy. In addition, although Mexico's economy crashed in 1994, right after NAFTA's ratification, U.S. exports to Mexico

remained relatively robust. How could this be given the sharp drop in the peso's value, and therefore in the purchasing power of the typical Mexican?

China has been touted as a huge export market for American producers as well. But its booming economy of the 1990s never accounted for more than 2.1 percent of U.S. goods exports during the decade.

B. The Widening Export-Investment Gap

Mystery markets, however, are far from the only evidence for the heightened prominence of investment considerations in U.S. trade policy. Also pointing to this orientation is the widening gap between U.S. exports and U.S. outward-bound direct investment.

As made clear by research published by the U.N. Conference on Trade and Development, this growing gap is a global phenomenon. The output of corporate international production networks and the sales of the foreign affiliates of multinational companies have been growing much faster than exports for the past two decades, and are now nearly twice as high.

The United States has been no exception to this rule. From 1994 to 2000, for example, U.S. goods exports increased 52.3 percent, and U.S. manufactured exports increased 56.1 percent. Yet the value of U.S. direct investment abroad for all industries (measured on an historic cost basis) more than doubled during this period. The comparable figure for manufacturing industries rose just over 71 percent.

For specific countries, the trends are even more striking, and lend considerable support to the argument that U.S. foreign investment is more strongly associated with net increases of U.S. imports than with net increases of U.S. exports—and with larger, not smaller, U.S. trade deficits. China—America's most difficult trade policy partner—is the most striking example.

From 1994 to 2000, U.S. total goods exports to China rose by 74.9 percent, and manufactured exports rose by 71.7 percent. But the value of total U.S. total direct investment in China surged nearly 275 percent during this period, and the value of manufacturing investment shot up by more than 466 percent. Not surprisingly, U.S. total goods imports and manufactures from China over these years each rose by 158 percent—more than twice as fast as U.S. export growth.

The supremacy of investment considerations in U.S.-China trade can also be gleaned from what U.S. multinationals themselves say about their economic dealings with China and their priorities vis-a-vis the People's Republic. A study of the websites of more than forty leading U.S. multinational companies I published last spring revealed that most of the major U.S. firms engaged economically with China are thinking primarily of investing and producing in China, not exporting from the United States to China.

Some of these companies have even publicly stated their intention to help China replace imports (from anywhere in the world, including the United States), with domestic production. Kodak, for example, reports that its manufacturing operations in China support Beijing's determination to "create professional enterprises which could displace imports and boost tax revenues." According to Westinghouse: "By using Westinghouse technology and domestic manufacturing sites, China will greatly reduce its need to import power-generating equipment." Similarly, companies like Compaq, Motorola, and Procter & Gamble are all on record pledging to raise the Chinese content of their products.

In fact, in September, 1999, Kodak's chief of China operations made crystal clear how the company views the roles played by exports from the United States and investments in China: "We believe that viewing emerging markets only as export opportunities is the wrong strategy. In a market such as China, where the value of business is expected to grow rapidly, local manufacturing is simply a better business model." Just 3 months earlier, testifying to the House Ways and Means Committee on China's WTO application, Kodak CEO George Fisher contended that "Kodak factories in China will be important customers for Kodak exports made in the United States."

IV. WHY THE INVESTMENT-TRADE DISTINCTION MATTERS

The importance of properly distinguishing between export-oriented and investment-oriented trade agreements is best revealed by the U.S. Government's recent failures accurately to project the economic impacts of the trade agreements it has sought.

As previously discussed, NAFTA was sold primarily to Congress and the public as an export booster. Not only did Presidents Bush and Clinton and their top aides speak in these terms, but during the Bush administration, two government studies reenforced this case. The first was undertaken by the U.S. International Trade Com-

mission. The second was conducted for the Labor Department by University of Maryland economist Clopper Almon.

These studies dutifully examined the likely impact on U.S. trade flows and balances of reducing Mexico's tariff barriers and even its non-tariff barriers. Both predicted modest gains for the United States on these grounds. Yet neither study examined the likely impact of the changed North American and global investment flows that NAFTA would surely bring—even though Mexico supported NAFTA expressly to lure desperately needed foreign investment. As a Congressional Research Service specialist warned diplomatically in 1991, trade studies that ignore investment effects are of limited utility.

The Bush administration promised extraordinary gains from a Uruguay Round agreement as well. It studied the likely economic impact even less extensively than its scrutinized NAFTA, but the results and problems were similar. In fact, most of the administration's economic case for the Uruguay Round rested on a report prepared by Australia's Centre for International Economics, whose only mention of investment was the completely unrealistic assumption that a new trade agreement would be accompanied by an instantaneous rationalization of the world's labor and capital assets.

And despite the enormous impact on investment flows almost universally expected from China's entry into the World Trade Organization, the USITC's August, 1999 investigation of this development's "economic effects on the United States" lacked any comprehensive discussion of investment issues. And almost completely ignored was the relationship between investment flows and export flows.

V. CONCLUSION

It is possible, though doubtful, that voters and legislators want American Presidents to negotiate trade agreements that ignore one of the most important features of the world economy—rapidly rising flows of foreign direct investment. As a result, it is possible, though doubtful, that voters and legislators want American Presidents to negotiate trade agreements bound to send more of our production abroad than they generate at home. And it is possible, though doubtful, that voters and legislators want American Presidents to negotiate trade agreements that add significantly to our trade deficits and therefore undermine our nation's financial future.

But whatever our views of the recent successes or failures of U.S. trade policy, I hope we can all agree that voters and legislators at the least should be told explicitly that such decisions are being made. There can be no excuses for hiding the truth.

The CHAIRMAN. Thank you very much.

Mr. REINSCH.

STATEMENT OF WILLIAM REINSCH, PRESIDENT, NATIONAL FOREIGN TRADE COUNCIL, ON BEHALF OF THE NATIONAL FOREIGN TRADE COUNCIL AND THE ORGANIZATION FOR INTERNATIONAL INVESTMENT

Mr. REINSCH. Thank you very much, Mr. Chairman. It is a pleasure to be back. I appreciate the opportunity to present the views of the National Foreign Trade Council, as well as the Organization for International Investment.

The growing importance of international investment is a natural consequence of the globalization that has been the hallmark of the world economy for the past two decades.

Simply put, no business any longer has the luxury of limiting its view to its own back yard. Today's business environment, with its technological advances, multiple market possibilities, industry alliances, and greater consumer sophistication, demands that all companies compete through investment-led strategies.

Some critics charge that the investment flows encouraged by the rules-based system amount to nothing more than the exportation of American jobs, and it is by now an article of faith in the anti-globalization movement that investment flows are inexorably

drawn to low wage countries with lower protections for labor, the environment, or human rights.

However, if that were true, one would expect the least developed countries to have been the recipients of massive investments in the last decade. The facts do not support that rhetoric, however.

The United States, which receives more than 30 percent of worldwide investment, has been almost certainly the greatest beneficiary of the explosion in international investment during the past decade. Let me present a couple of facts taken from my written statement.

U.S. affiliates of multinational companies sent nearly $900 billion into the U.S. economy in the 1990s. U.S. subsidiaries of foreign companies employ 5.6 million Americans and pay average annual salaries of over $46,000, well above the average salary for U.S. workers as a whole. For the past 5 years, U.S. subsidiaries of multinational companies have paid record levels of Federal taxes. In 1997, a record $19.7 billion was paid, a 28 percent increase over the previous year. U.S. subs of foreign companies exported a record $150.8 billion worth of merchandise in 1998, representing 22 percent of all goods exported by the United States.

Mr. Chairman, my written statement has a lengthy section on the value of and advantages of inward investment using the State of South Carolina as an example and citing much of your work when you were Governor. In the interest of time, I am going to skip that part, but you are welcome to read it when you have the opportunity.

In addition, though, looking at another angle, the geographic destination of U.S. foreign investment has not changed over a long period of time. Europe continued to account for nearly 55 percent of the total U.S. foreign direct investment during the last 10 years. Within the Asia Pacific region, U.S. firms did not favor China, the second largest market in the region, but rather Australia, which is a smaller market than many U.S. States.

Today more than 75 percent of all foreign direct investment is in the developed world. In fact, investment has raced to the top, flowing in overwhelming proportion to stable democracies that are characterized by high living standards, well developed regulatory regimes, and transparent legal systems.

U.S. outbound investment also promotes U.S. export industries. Increased levels of foreign investment and foreign sales are magnets for U.S. exports. According to the survey of current business, exports by U.S. multinationals were $438 billion in 1998, an amount equal to some two-thirds of all U.S. exports. More than 40 percent of exports were to majority-owned affiliates of those U.S. companies.

We believe rules-based trade agreements contributing to international investment flows lead to increased exports of goods and services and make a substantial contribution to the economic well-being of our country as a whole. There are many examples of high quality, high paying American jobs that are directly tied to the expansion of U.S. trade and investments.

One is GE Power Systems, a $15.2 billion global business headquartered in Atlanta. GE recently announced that construction is underway at the Baglin Bay power station in South Wales,

which will supply electricity and steam to industrial and commercial facilities there.

The cornerstone of that system is a 50-hertz gas turbine which was shipped from GE's South Carolina plant last December. That plant employs approximately 2,900 people. But the story does not end with the gas turbine, which is the highest technology component in this project. Other components key to making the plant work, for example, include a gas generator supplied by GE's plant in Florence, Italy.

In other words, interdependence is a business norm in the global marketplace. It is no longer rare to find that jobs or economic welfare of a company in a small Midwest town is tied to successful operation of its foreign affiliate in Europe or in Asia. The good news has been and remains that these transnational economic relations are winning propositions for the people on both ends of the equation.

This hearing asks whether trade agreements are really investment agreements. The real question, we believe, is whether trade agreements cause U.S. companies to invest abroad. The data suggests for us that the answer is no.

However, if the Committee is concerned about artificial influences on U.S. companies' decisions to invest abroad, then I would suggest two other questions that you might want to consider in future hearings.

One is do trade barriers force firms to invest abroad?

Some companies have been forced to invest in manufacturing abroad in order to overcome government trade barriers on the raw materials they use or as a market entry strategy to surmount protectionist barriers to their finished products.

This certainly applies to some foreign direct investments in places like China, Brazil, and India. How many U.S. companies could have supplied these markets from their U.S. operation?

How many more jobs would be supported if we could lower the tariffs and non-tariff barriers that some nations have erected? Secretary Evans' written statement, Mr. Chairman, has an example taken from Brazil and the automobile industry that I think is illustrative of the point I just made.

A second question is whether trade agreements that other countries are concluding are driving U.S. companies to invest abroad. My statement elaborates a little bit more on that point as well. We believe that location decisions that multinational companies make take into account the trade treatment of goods and services from each of their facilities, along with production costs and transportation expenses.

U.S. Trade Representative Robert Zellick illustrated this very well at an NFTC lunch last week with the story of Caterpillar's motor graders. Their Illinois-made motor graders face nearly $15,000 in tariffs when they are exported to Chile. When Caterpillar manufactures the same item in Brazil for export to Chile, the tariff is $3,700, and when Caterpillar's competitors make them in Canada they can be exported to Chile free of tariffs, in other words zero duty, because of the Canada-Chile Free Trade Agreement.

This is the kind of disparity in trade barriers that, among other things, encourages companies, American companies, to locate off-

shore and which I think distorts trade, and which trade agreements, including the ones that we have had under discussion today, are designed to deal with.

In conclusion, Mr. Chairman, I believe trade agreements lower artificial government barriers to trade and thus allow companies to make manufacturing, location and production decisions under clearer economic conditions.

Multinational companies' decisions in regard to their global supply chain are a complex calculation involving work force quality, transportation access and cost, proximity to key suppliers or customers, and the overall business climate in a location.

Trade barriers do skew that calculation, often to the detriment of the United States. Trade agreements that lower those barriers will let U.S. manufacturers, like Caterpillar's motor grader plant in Illinois, compete on a level playing field both against other related manufacturing locations abroad and against those of their competitors.

Thank you very much.

[The prepared statement of Mr. Reinsch follows:]

PREPARED STATEMENT OF WILLIAM REINSCH, PRESIDENT, NATIONAL FOREIGN TRADE COUNCIL, ON BEHALF OF THE NATIONAL FOREIGN TRADE COUNCIL AND THE ORGANIZATION FOR INTERNATIONAL INVESTMENT

Mr. Chairman, thank you for the opportunity to present the views of the National Foreign Trade Council (NFTC) and the Organization for International Investment (OFII) on how trade and investment flows are intertwined and how international trade and investment agreements affect corporate decisions about their global supply and production chains.

The member companies of both the organizations that I represent today, while different in the locations of their headquarters, are united in their support of the rules-based trading system. Most of the NFTC's members are U.S. based firms that trade and invest around the world. OFII's members are the U.S. subsidiaries of companies based abroad that are likewise active participants in the global trading system. While many of our members compete in a particular industry or sector, they broadly share a common view of the rules under which they compete: non-discrimination for foreign investors (national treatment), non-discrimination between goods imported and goods made domestically, multilateral agreement to limit the use of government subsidies, and protection of intellectual property. They support these rules in their home markets and seek them when trading abroad.

The growing importance of international investment is a natural consequence of the globalization that has been the hallmark of the past two decades. Whether searching for opportunities or looking out for competitors, business no longer has the luxury of limiting its view to its own backyard. Today's business environment, with its technological advances, multiple market possibilities, industry alliances, and greater consumer sophistication, demands that all companies compete through investment-led strategies.

Some critics charge that the investment flows encouraged by the rules-based system amount to nothing more than the exportation of American jobs. Others claim that under a liberalized trade regime, investment always flows downhill to the lowest wage-earning countries with minimal environmental protections, the so-called "race to the bottom." In truth, the expansion of direct investment by both U.S. and non-U.S. companies has contributed substantially to the economic health of the United States, while helping to lift many other developed and developing countries to new heights of prosperity. We believe that international investment and trade, conducted under the rules-based trading system is a force for economic growth, democracy, stability and is of direct economic benefit for millions of individuals around the world.

It is by now an article of faith in the anti-globalization movement that investment flows are inexorably drawn to low-wage countries with lower protections for labor, the environment, or human rights. However, if that were true, one would expect the least developed countries to have been the recipients of massive investments in the last decade, but the facts do not support the critics' rhetoric.

THE UNITED STATES: LARGEST RECIPIENT OF FOREIGN INVESTMENT

The United States has been almost certainly the greatest beneficiary of the explosion in international investment during the past decade. U.S. affiliates of multinational companies, which number more than 9,700 companies, infused nearly $900 billion into the U.S. economy in the 1990s, more than the amount invested over the previous four decades combined. Today, the United States receives more than 30 percent of worldwide investment. According to the Commerce Department's Bureau of Economic Analysis, foreign investment in the United States was almost $317 billion last year. Once in the United States, U.S. subsidiaries continually reinvest a significant portion of their U.S. earnings back into their American operations. In 1999, they reinvested 53 percent of their earnings, totaling a record $18.8 billion. They also make significant investments in research and development and in new plants and equipment, all of which provide business to other companies in the United States. In 1998, U.S. subsidiaries spent a new high of $25.2 billion on U.S. research and development activities conducted by American scientists and engineers and supported by U.S. suppliers and sub-contractors.

In perhaps the best evidence of their impact, U.S. subsidiaries of foreign companies employ 5.6 million Americans and pay average annual salaries of over $46,000, well above the average salary for U.S. workers as a whole. They account for 13.5 percent of all U.S. manufacturing jobs. For the past 5 years, U.S. subsidiaries have paid record levels of Federal taxes. According to the most recent IRS statistics (1997), foreign companies paid a record $19.7 billion in Federal taxes, a 28 percent increase over the previous year.

In addition, U.S. subsidiaries exported a record $150.8 billion of merchandise in 1998, representing 22 percent of all goods exported by the United States. In fact, U.S. subsidiaries have accounted for at least 20 percent of U.S. exported goods for all but one year since 1980. America's low trade barriers and open investment policies are significant reasons why these companies choose the United States as a location, not just to service our market, but as an export platform to other markets.

Beyond the clear benefits of both the direct and indirect jobs provided by U.S. subsidiaries, there is a new set of stakeholders in the U.S. who also derive personal benefit from the operations of these companies here and abroad: shareholders. A recent study, commissioned by OFII and Citibank, tracked the 100 publicly traded foreign-based companies whose subsidiaries generated the most U.S. sales. The study found U.S. investors own 20 percent of the total shares of these 100 companies. Among them, 62 have U.S. investors holding 10 percent of shares and U.S. ownership is as high as 30 percent or more for 22 of the companies. Nokia is a perfect example of one such foreign-based company with a major presence in the United States. It provides one of America's best selling cell phone brands, with over 5,500 U.S. employees in its Texas manufacturing operations. But the United States has another significant stake in the company: today, U.S. investors own 55 percent of Nokia's stock.

SOUTH CAROLINA: A FOREIGN INVESTMENT SUCCESS STORY

The benefits that accrue to Americans from the domestic investments of foreign companies can be seen not simply in quantitative data and upwardly sloping economic statistics, but in the stories about real changes in the quality of people's lives.

Mr. Chairman, we need not look further than your home State to witness how international investment has contributed to our economy. The story of foreign investment in South Carolina dates back to your tenure as Governor when you began to build the solid foundation of the excellent business climate the State enjoys today. As a result, in part of your creation of a statewide network of technical colleges that emphasizes job training and your commitment to fiscal responsibility, South Carolina enjoys one of the lowest unemployment rates in the country.

The flood of blue chip international companies that have chosen South Carolina as a manufacturing location is remarkable if viewed historically. In the past, among the State's largest sources of employment were textile production and garment manufacturing. Fast-forward to today and you see a remarkably different economic landscape. Textile manufacturers still provide significant employment, but are driven by the engine of their investment in high-tech automation. Down the street from the new textile mills, sit the manufacturing operations of companies from around the world. According to Department of Commerce figures, the State now has 116,900 jobs supported by U.S. subsidiaries, 66,800 of which are in manufacturing, a 77 percent increase over 10 years.

One of the best examples of South Carolina's efforts to attract international companies is BMW Manufacturing's arrival in 1992. The luxury German carmaker, with a devotion to quality, was not looking for cheap labor or to get around a tariff wall.

They were looking for a place to build a new type of car: the Z3. They wanted a location that would be a global center of excellence. The vehicles produced were not to be mere kits made in Germany to be slapped together in South Carolina, but top-of-the-line automobiles manufactured basically from the tires up in the State.

BMW could have put this plant anywhere. It would have been easier to simply build it in Germany or elsewhere in Europe. If they were looking for cheap labor in the Americas or to surmount trade barriers, post-NAFTA Mexico would have been an obvious choice. But they did not. They chose South Carolina because of its educated workforce, the low cost of land and welcoming business environment. As part of their decision matrix, transportation was also central: getting components from around the country and the world in a timely fashion, while also exporting the finished cars to markets around the world, BMW needed good transportation options. The history of bringing BMW to South Carolina is now legend, but in this area, one of your efforts stand out: securing more than $45 million to facilitate BMW's needs at the Greenville-Spartanburg International Airport, thus helping attract the company to the State.

At the end of the day, BMW's decision to locate in South Carolina delivered significant economic benefits. According to the company, BMW Manufacturing Corp. has made a total investment of $1.675 billion in the State, paid total compensation of $699.2 million and paid taxes and duties of over $190 million. Most significantly are the nearly 8,000 people that are directly employed there where the average worker can earn salaries that top more than $56,000 a year. Additional jobs—approximately 4,700—are attributed by BMW to the suppliers who have come to the State with a "multiplier" economic impact of $1 billion.

U.S. INVESTMENT ABROAD SUPPORTS JOBS AT HOME AND DEVELOPMENT ABROAD

As much as companies abroad have invested at record levels in the United States, U.S. firms have kept apace in their overseas investments, investing $802 billion during the 1990s, more than they had in the prior four decades combined. But for all the talk of the "Asian tigers," new Eastern European markets, China's liberalizing economy, or India's economic reform, the geographic destination of U.S. foreign investment has not changed. Europe continued to account for nearly 55 percent of the total U.S. foreign direct investment during the last 10 years. Within North America, Canada received 8 percent of U.S. outbound investments, drawing $2 of U.S. investment for every $1 invested in Mexico since 1994. Within the Asia-Pacific region, U.S. firms did not favor China, the second largest market in the region, but rather Australia, which is a smaller market than many U.S. states. Australia attracted 20 percent of the total U.S. investment in the Asia-Pacific region because of its educated workforce, legal protections, and technological capabilities. U.S. multinationals' investment strategies are much more motivated by access to affluent markets, skilled labor, and technological advantages than the possibility of reducing wages.

Today, more than 75 percent of all foreign direct investment is in the developed world. As noted, the United States itself is host to more than 30 percent of all such investment. The United Kingdom runs a distant second with a little more than one-fourth the total of the United States or $82 billion as of 1999. China, by contrast, received only $40 billion in 1999, less than 5 percent of global flows. Thus, investment has, in fact, raced to the top, flowing in overwhelming proportion to stable democracies that are characterized by high living standards, well-developed regulatory regimes, and transparent legal systems.

Statistics on wages similarly belie the anti-globalization rhetoric. In 1998, the average compensation paid to workers at majority-owned U.S. affiliates throughout the world was $33,100. In Canada and Europe, the average compensation at these subsidiaries topped $41,200. Investment simply has not "raced" to the lowest wage levels.

Nor is it true, as critics often claim, that U.S. firms' foreign workforce is concentrated in developing countries with low wages and poor conditions. In fact, the vast majority of people employed by U.S. affiliates live in other wealthy, developed countries. In Europe, U.S. affiliates employed roughly 3.5 million workers in 1998—more than the combined U.S. workforce in Latin America and developing Asia. Almost a million Canadians are employed by U.S. subsidiaries—more than four times the number working in China.

U.S. FOREIGN INVESTMENT PROMOTES EXPORTS

U.S. outbound investment also promotes U.S. export industries. As of 1998, the assets of non-bank foreign affiliates of U.S. companies exceeded $4 trillion. In the same year, non-bank foreign affiliates of U.S. companies had over $2.4 trillion in

sales in their domestic markets, nearly two-and-one-half times the amount of U.S. exports of goods and services. And these increased levels of foreign investment and foreign sales pull U.S. exports. According to the Survey of Current Business, exports by U.S. multinationals were $438 billion in 1998, an amount equal to some two-thirds of all U.S. exports. More than 40 percent of exports were to the majority-owned affiliates of those U.S. companies. Thus, rules-based trade agreements contributing to international investment flows do not export jobs, but rather lead to increased exports of goods and services and make a substantial contribution to the economic well-being of our country as a whole.

THE ECONOMIC RETURNS FROM U.S. FOREIGN INVESTMENT

U.S. investment overseas reaps significant economic returns for Americans through higher employment levels in the United States, more sources of revenue, and improved productivity. There are countless examples of high-paying, quality American jobs that are directly tied to the expansion of U.S. trade and investment. Consider the example of GE Power Systems, a $15.2 billion global business with operations around the world and throughout the United States. GE Power Systems is headquartered in Atlanta, GA, but has major operations in Greenville, SC; Belfort, France; Houston, TX; Florence, Italy and Schenectady, NY to name just a few.

GE recently announced that construction is well underway at the Baglan Bay Power Station in South Wales, site of the world's first GE H System. The 480-megawatt Baglan Bay Power Station will supply electricity and steam to industrial and commercial facilities within the new Baglan Energy Park, with excess power bid into the U.K. grid. The Energy Park is one of the largest single areas of industrial development in the U.K.

The cornerstone of the GE H System is the 50-hertz MS9001H gas turbine, which was shipped from GE's Greenville, SC gas turbine manufacturing facility in December of 2000. The H System will produce 480 MW of electricity, enough to power 168,000 homes. It will be fueled by natural gas. Gas powered turbines used for power generation are similar to jet aircraft engines, but on a larger scale.

The GE Power Systems Greenville plant is the largest and most advanced heavy-duty gas turbine production facility in the world. At the facility, GE has the capacity to produce large gas turbines ranging in size from 40 to 480 MW used for generating electric power around the globe. The facility employs approximately 2,900 people and is the largest exporter of manufactured goods in South Carolina.

But the story doesn't end with the highest technology component, the gas turbine from South Carolina. Other components are key to making the Baglan site work, for instance the plant will use a GE LM2500 gas generator supplied by GE Nuovo Pignone in Florence, Italy.

Interdependence is a business norm in the global marketplace. It is no longer rare to find the jobs or economic welfare of a company in a small Midwest town tied to the successful operation of its foreign affiliate in Europe or Asia. But the good news has been and remains that these transnational economic relations are winning propositions for the people on both ends.

Conclusion

This hearing asks whether trade agreements are really investment agreements. The real question is whether trade agreements cause U.S. companies to invest abroad. The data I have presented suggests the answer is: "no." However, if the Committee is concerned about artificial influences on U.S. companies' decisions to invest abroad, then we might suggest two other questions for future Committee hearings:

"Do trade barriers force firms to invest abroad?" Some companies have been forced to invest and manufacture abroad in order to overcome government trade barriers on the raw materials they use or as a market entry strategy to surmount protectionist barriers to their finished products. This certainly applies to some foreign direct investments in places like China, Brazil and India. How many U.S. companies, that desire to compete in every major market, could have supplied these markets from their U.S. operations? How many other international investors in the U.S., like BMW, would be able to use their U.S. operations as an export platform to South America if we had successfully completed the Free Trade Agreement for the Americas (FTAA) in the last Administration where the negotiations started? How many more jobs would be supported if we could lower the tariffs and non-tariff barriers that some nations have erected?

"Are the trade agreements that other countries are concluding driving U.S. companies to invest abroad?" The United States has been falling behind in negotiating trade agreements that lower barriers for U.S. goods and services. Today, the European Union has 27 free trade or special customs agreements around the world, 20

of which it negotiated in the 1990s; it is negotiating another 15 right now. Countries throughout East Asia are quickening the pace of special trade negotiations. Japan is negotiating a free trade agreement with Singapore, and is exploring free trade agreements with Canada, Mexico, Korea, and Chile. In our own hemisphere, there are 30 free trade agreements, and the United States is party to only one.

We believe production location decisions for multinational companies take into account the trade treatment of the goods and services from each of their global locations along with production costs and transportation expenses.

U.S. Trade Representative Robert Zoellick illustrated this very well at a lunch hosted by the NFTC last week. He told the story of Caterpillar and the motor graders they make in Illinois. Caterpillar's Illinois-made motor graders face nearly $15,000 in tariffs when exported to Chile. When Caterpillar manufactures them in Brazil for export to Chile, the tariff is just $3,700. And when Caterpillar's competitors make them in Canada, it can be exported to Chile free of tariffs because of the Canada-Chile free trade agreement.

If we continue to miss out on the effort to lower trade barriers, we may find that U.S. based companies have little choice but to service some countries and whole regions from manufacturing sites outside the United States.

Mr. Chairman, contrary to the premise of today's hearing, trade agreements lower artificial government barriers to trade and thus allow companies to make manufacturing location and production decisions under clearer economic conditions. Multinational companies' decisions in regard to their global supply chain are a complex calculation involving workforce quality, transportation access and cost, proximity to key suppliers or customers and the overall business climate in a location. Trade barriers skew the calculation, often to the detriment of the United States. Trade agreements that lower these barriers will allow U.S. manufacturers like BMW's South Carolina plant and Caterpillar's motor grader plant in Illinois to compete on a level playing field both against other related manufacturing locations abroad and those of their competitors.

The CHAIRMAN. Thank you very much.

Dr. Luttwak.

STATEMENT OF EDWARD N. LUTTWAK, PH.D., CENTER FOR STRATEGIC AND INTERNATIONAL STUDIES

Dr. LUTTWAK. I want to thank the Senators on this Committee, because I am grateful for their continuing focus on this issue and for their continuing refusal to simply go along with the prevailing ideology. The last century was a great lesson in the power of ideology over man's minds. The ideology in question is the theory of comparative advantage.

We all know that the theory of comparative advantage is a perfectly valid theory as it was enunciated by Ricardo, but there is also another theory and that is the theory of political comparative disadvantage. In other words, what ought to happen in the world of economic theory is that we all do what we are best at doing, remove all barriers and impediments, and, geography aside, we will have a world which will be altogether more productive. Everybody would be richer.

What actually happens from time to time at any one moment in real life is that there is the phenomenon of what actually happens is not dictated by economic comparative advantage, it is dictated by it plus the interaction with political comparative disadvantage. In other words, groups that are politically weak are unable to do anything about it and they absorb whatever winds and tides and storms the world economy happens to hit them with, and groups that are politically strong, what they do is they garrison their sectors of the economy and they protect themselves.

It is, in my view, a credit to Japan that, if you look at Japanese protectionism, which is a very real phenomenon, it is weak groups

that are protected, it is marginal groups, the very groups that in our political system are completely ignored. It is craftsmen, traditional craftsmen, it is the small-scale farmer, the very people that in our system are ignored.

I think that what the Japanese are saying to us is that for countries that are wealthy, that have a high GNP, there is something more important than increasing the total GNP by another tiny percentage point if this means that you are going to have a substantive move away from an egalitarian to a more extreme distribution of income, or if it means you are going to lose pieces of your society, like traditional craftsmen. As you know, the very last fight between the Chinese and the Japanese has to do with protecting the importation of the straw sandals, a very old craft.

So, what I see the Senator and this Committee doing is intervening on the side of those who are comparatively disadvantaged in the normal political process. General Electric is not disadvantaged in the normal. General Electric is well represented in the political process, and I see the Senator and this Committee intervening on behalf of the industrial workers in less powerful industries and such like.

The second observation arises from having heard the dialog between Secretary Evans and Senator Hollings.

Senator Hollings starts off by saying: Look, we have a trade deficit which has become colossal, 4 percent of GNP, and this cannot be sustainable, and it is associated with all these phenomenon. Evans replies: Well, I go around the country, everybody is prosperous.

Well, the reason is that there are actually two different time perspectives at work. The process of decline that transformed Holland, which was an industrial, shipbuilding industrial country and trading and so on, into first it was industrial, then it became financial, and then it became nothing. That process of decline was not accompanied by drastic impoverishment. At any one time there was a bubble surface of prosperity.

In England, when I went to Great Britain in 1955, not only did the British have the highest GNP per capita in Europe, but also the distributed standard of living was such that the average Englishman lived much better than the average French, German, Italian. Well, today what happens is that the GNP per capita, of course, is much lower than it is in France or Germany. But, in fact, that depends upon the fluctuating pound to euro.

But what has happened is that the actual standard of living of the distributed population of England has declined catastrophically, so much so that when Italian industrial workers in part of a joint trade, development, investment, acquisition, industrial workers visit industrial workers in the British Midlands, they are stepping into what, for Italians, is a Dickensian world of people who live miserably by their standard.

In other words, the processes of long-term decline associated with de-industrialization are not visible at any one moment in time and it is only historically that—the Dutch woke up in the 19th Century having discovered that losing industry and gaining finance was not making it, even though the GNP would show very good results. The GNP does not measure what happens within economies.

The final point I would like to make is that, in regard to the large book of non-compliances, I think that the very same substantive outlook you have brought to this process, Senator should be focused at this moment on the civilian aerospace industry. There we have a real problem between Boeing and Airbus, and this is not just the wily processes by which, for example, the French Ministry of Transport budget flows into a subsidy for the super-jumbo because, you know, they are going to straighten the Bourdeaux-Toulouse Road and provide some money for these vehicles, much more focused substantively.

Perhaps what is fundamentally wrong is not unfairness on the part of Airbus subsidization, but the fact that Boeing is a monopoly. It is a sleep monopoly, or a stagnant monopoly, or a silly monopoly, or a mismanaged monopoly, but still, look at it substantively, the way Hamilton, who you so rightly quoted, told us to do. Hamilton said: I know, I understand the theory—because, of course, the theory was around long before David Ricardo specified it; it was implicit in Adam Smith and it was implicit 100 years before Adam Smith in the Martyn merchants thing on the India trade.

Hamilton said: "I know the theory, the theory is great; the only thing is, I do not want in the United States the kind of prosperity associated with successful plantations. I want it to have a distributed prosperity of many factories and so on."

In that vein of substantiveness, I think we should really look at the aerospace industry and see what has happened to it and whether the remedies are international. Probably the remedies would have to be much broader than that. They may involve antitrust. I do not know. But we have to do something, because it is a very important industry and it is clearly going down the drain.

Thank you.

[The prepared statement of Dr. Luttwak follows:]

Prepared Statement of Edward N. Luttwak, Ph.D., Center for Strategic and International Studies

[Extract from re-draft of *Turbo-Capitalism: Winners and Losers in the Global Economy* HarperCollins 1999, Harper Perennial, 2000]

Free Trade As Ideology

[By Edward N. Luttwak]

The god of the market-worshippers is Adam Smith, a devotion that crucially depends on not reading him. Being far wiser than his modern worshippers, Smith filled his work with exceptions, exclusions and reservations to the rule that free markets allocate most efficiently, maximizing the common welfare. As for the specific worship of free foreign trade—a varitable religion for the American and British ruling elites—it is just as important not to read either Adam Smith or his worthy predecessor, Henry Martyn, merchant in the East India trade, a pithy writer, he was excessively clear-minded thinker from the viewpoint of today's true believers. Unlike them, Martyn recognized that wealth may point in one direction, welfare in another.

Seventy-five years before Adam Smith published his *Inquiry Into the Nature and Causes of the Wealth of Nations*, seventy-seven years before Adam Smith became a commissioner of customs in Edinburgh through the influence of the Duke of Baccleuch, thereafter commending the bravely independent risk-taking of free enteprise and the superiority of unrestricted free trade while holding a secure government post charged with obstructing imports into Scotland, Henry Martyn's *Considerations Upon the East India Trade* of 1701, written to oppose the East India

Company's monopoly, had already anticipated most of what is right and wrong about the theory of free trade:

"Things may be imported from India by fewer hands than as good would be made in England, so that to permit the consumption of Indian manufactures is to permit the loss of few men's labor . . . A law to restrain us to use only English manufactures, is to oblige us to make them first, is to oblige us to provide for our consumption by the labor of many, what might as well be done by the labor of few, is to oblige us to consume the labor of many when that of few might be sufficient."

Martyn captures the opportunity-cost essence of the free trade argument lucidly enough:

"If nine cannot produce above three bushels of wheat in England, if by equal labor they might procure nine bushels from another country, to employ these in agriculture at home, is to employ nine to do no more work than might be done as well by three."

That is what is right about free trade theory. Import barriers artificially preclude efficiency gains identical to those achieved by better technology, better organization or any other source of domestic productivity. That goods or services originate from a point on the surface on the planet that happens to be classified as foreign at a given time (subject to change by conquest or voluntary union), is an entirely meaningless attribute in purely economic terms. Until the late 195Os, there were still tariff (*Dazio*) barriers *within* Italy, so that trade-foreigners were as near as the next town.

Equally, all that is wrong about free trade is already evident in Martyn's pamphlet:

"If the same work is done by one, which was done before by three; if the other two are forced to sit still, the Kingdom got nothing before by the labor of the two, and therefore loses nothing by their sitting still."

In other words, what benefits the Kingdom, or the Gross National Product as we would now say, need not benefit all its subjects, and may indeed turn some into paupers. Of course the same is true of any other increase in efficiency, such as might ensue from the use of better software for example. But simply because any change in trade barriers is a matter of presumptively democratic *political* decisions, unlike changes in computer usage done by private firms or individuals for their private reasons with private funds, the employment implications cannot be overlooked.

In poor countries, free trade can drastically alter the total economy given favorable circumstances including foreign investment, lifting much of the population to a much higher levels of income. In affluent countries, however, long on total national wealth, but now increasingly afflicted by the return of poverty in the most vulnerable fraction of their populations, it is not necessarily a good idea to enrich the Kingdom by replacing three with one, leaving the other two "sitting still".

Most economists would, of course, immediately point out that it is much better for all if the many gainers from any given market opening compensate the few losers, rather than to keep protectionist barriers that reduce the total incomes of all. They say that, sometimes offering a quick calculation—and then they leave the scene. That some workers may be protected by some trade barriers while compensation schemes are *never* implemented, is a political phenomenon outside the scope of the profession as now defined. For they who invoke the Master have abandoned his broad political economy for an abstract economics of "other things being equal", and purely theoretical compensations for any adversities.

In particular, most contemporary economists simply ignore the possibility that people might actually prefer to live in a country whose economy is somewhat less efficient than it could be, because of protectionism among other impediments. In fact, they implicitly assume that societies exist to serve the needs of their economies, instead of the other way round, thereby attributing no importance to the stability of employment (as opposed to earning levels), the upkeep of traditions (e.g. Japan's rice-farming culture), or the avoidance of gross increases in the inequality of incomes and wealth.

True, many of those who attack the ruling orthodoxy go beyond societal welfare-versus-wealth arguments, intrude into purely economic analyses, and in so doing keep repeating the same elementary errors. They persistently and grossly over-estimate the importance of international trade and investment flows for the national economies of major countries, and most notably for the huge American economy. In this "turbo-capitalism" critique of mine, by contrast, globalization ranks as a distant fourth after privatization, de-regulation and technological change.

Most commonly, the errant opponents of free trade keep confusing competition among goods with wage competition. It is each country's internal labor market that sets wages, so that, say, German workers whose employers are competing head-to-head with, say, Indian exports are not themselves competing with Indian workers,

whose own wages are quite irrelevant to their own. Only the competition of other German workers matters—so that Indian exports can affect the wage rates of German workers indirectly, insofar as an unfavorable trade balance rather than any other reason causes unemployment reducing wages (in Germany's case only in theory, because German wages are kept downwardly rigid by trade-union power).

Some opponents of free trade are so overcome by their eagerness to translate cold war animosities into "geo-economic" rivalries that they miscontrue them as *national* confrontations. Yet for each Boeing-Airbus Industrie truly zero-sum market war over airframes there is a American GE-French SNECMA alliance of engine manufacturers. Because for each major country the strongest trading competitors are also routinely the largest export customers, geo-economic rivalries are destined to remain strictly confined to the specific industries involved, without descending into emotional national rivalries. And moreover, most amazingly, even supposedly trained economists tend to reveal an inability to understand the ancient and elementary theory of comparative advantage when arguing against free trade. The advantages in question are *internally* comparative, so that even if Lazo is less efficient than Worko in producing everything, its least-bad industries can still profitably export to Worko, whose own resources are best employed by its better industries, not the weakest industries with which Lazo is competing.

But there is more to it than that. Most advocates of free trade do not merely oppose trade barriers, they are offended by them. For they know that only the free interplay of supply and demand, a.k.a, the invisible hand, can set market-clearing prices with neither waste nor contrived shortages, thereby signalling to all producers what is the most efficient use of their scarce resources at any one moment in time. And they are frustrated in their knowledge that if all trade barriers were removed, the planetary income and standard of living would swiftly and greatly increase, because every producer would be free to fully exploit its own particular comparative advantages, eliminating a planet's worth of inefficiencies large and small. Instead, every state in the world artificially segments the planetary market, by imposing its own obstacles to imports by way of prohibitions, quota limits or tariffs—and sometimes to exports as well, often by pretending that only processed and not raw materials be sold abroad. Each state thus distorts not only its own internal market, but by successive displacements of supply and demand, all markets, everywhere. By so doing, the entire world's efficiency in using scarce resources is diminished, leaving the planet much poorer than it need be.

Because all competent academic economists know these things to be true, and because so little else in their inventory of theories remains unrefuted, most economists are greatly irritated by any and all arguments for trade barriers. In addition to proving them costly for the standard of living, they are eager to expose them as the spurious excuses of domestic producers, out to exploit the consumer by raising prices behind the shelter of import barriers.

When it could still be argued that food self-sufficiency was a strategic necessity, most economists asked why the agricultural interest should be allowed to levy its own permanent tax on all consumers, given that a one-time accumulation of reserve stocks of imported food would be far cheaper.

When it is argued that a particular industry could eventually become competitive if it can first grow to stength behind protective barriers, most economists assert that long-term lenders can finance the infancy of any industry far more efficiently than captive consumers. Nor would they ask for the indefinite continuation of enervatingly profitable import barriers, as protected industries always do.

When it is pointed out that import barriers can preserve employment, most economists trot out the compensation counter-argument, as if that theoretical construct were a practical remedy.

The emotional intensity of the free traders is particularly evident when they are confronted by important defectors from their own ranks. Richard Cobden lamented on his deathbed not his own imminent death, but rather John Stuart Mill's apostasy in formulating the infant-industry argument:

"I believe that the harm which Mill has done to the world by the passage in his book on *Political Economy* in which he favors the principle of protection in young communities has outweighed all the good which may have been caused by his other writings."

Alfred Marshall was no less mournful over the same defection:

"When John Stuart Mill ventured to tell the English people that some arguments for protection in new countries were scientifically valid, his friends spoke of it in anger—but more in sorrow than in anger—as his one sad departure from the sound principles of economic rectitude".

This is not so harsh as Cobden's condemnation, but equally replete with sentiment. It was just the same with Keynes. Originally he was the purest of the pure:

"We must hold to Free Trade, in its widest interpretation, as an inflexible dogma, to which no exception is admitted even in those rare cases where by infringing it we could in fact obtain a direct economic advantage." But Keynes too was to deviate from the path of economic rectitude. Reacting to Britain's very high unemployment rates after 1930, knowing that the government would not devalue sterling and that the unions would not accept wage reductions, Keynes "reluctantly" proposed tariffs as the only remaining method of increasing employment, through import substitution. That utterly dismayed his earstwhile friends, colleagues and admirers, some of whom reacted with outright hostility. Lionel Robbins (my own teacher) spoke of Keynes's "extraordinary naivete'" in believing that import duties could easily be removed *once they had served their purpose*. At the time, millions were living on the dole, eating bread and jam for breakfast, lunch and dinner, but Keynes's opponents worried about the distortions that might linger in the aftermath, perhaps years later.

After accepting in full every possible objection, including the marginality of all foreign trade and investment in very large economies, Keynes has the last word: one should do what one can, even at the expense of sacrificing abstract principle for mere flesh and blood.

The CHAIRMAN. It is going down the drain, Dr. Luttwak. It is interesting you observe it, because we just had last week a lunch with Mr. Bernie Schwartz of Loral and he was talking about aerospace and space satellites. He was noting that the two largest European producers were merging together and, with subsidies, they were going to take over that market.

Now, what you commented upon is just that. When you say the governmental political comparative disadvantage, you are exactly right. The comparative advantage is government and whatever the government policy is, and if the government policy is in Japan to take care of the weak, fine, it is working.

In fact, if I was the emperor of Japan I would continue to work it the same way. It is working. They have not had all the bankruptcies. They have taken over a larger share of our automobile market. Their economy grows stronger and stronger. I know about all the lament in *The Wall Street Journal* and everything else like that, but you can talk to others that are there and the people have gone along. The workers are paid far more than our industrial salaries, and it is working.

With respect to taking care of the weak, the weak are the textiles, the strong are the movies. Everybody is talking about intellectual, intellectual, we have got to sell Hollywood movies, but they do not talk about the workers in the textile plants.

Right to the point, Mr. Reinsch, about these jobs, you cite all these wonderful things about South Carolina. Yes. I really have been carpetbagging Schenectady, New York, with GE to bring it down to Greenville, where we have got the 2900. I have said openly I would rather have that GE than have Microsoft, because my GE workers probably make around $24 an hour, way more than the average. Well, if you are in charge of software that is a different thing, but I mean the average worker.

They had to go on strike out there to get retirement benefits in Seattle, at Microsoft.

So my GE workers are well paid and that is the middle class. My BMW workers are well paid. My problem is I had five GEs, now I have only got two. They told the GE plant in Labson, South Carolina that also made turbines, the Brazilians said, "we are not going to buy it unless you move."

So they have gone to Brazil.

The same with—I could go down the list of all the other plants. I looked at the fact the other day that we have had since NAFTA a net loss of 35,000 manufacturing jobs.

True, we have got Hoffman-LaRoche, Hitachi, Fuji, BMW, and GE has expanded and everything of that kind. But where I had all those GEs, I am down to two. Where I used to have four Westinghouse, I am down to two. Where I used to have four Duponts, I am down to two.

I have seen them come and then I have seen them go. I am watching this closely and I am having a net loss. There is no question—there is one thing I want in the record, because you helped produce it with the late Senator John Heinz with respect to Smoot-Hawley. I never have been able to get an official record around this place, but we need it before the Committee.

It was just mentioned by a previous witness that the GNP—the Secretary of Commerce—that 25 percent of our GNP was in world trade. At the time of Smoot-Hawley, only 1 percent, according to Mr. Reinsch of Senator Heinz's staff, and only one-third of the trade was affected by Smoot-Hawley. Two-thirds of the trade was not affected by Smoot-Hawley and it suffered just as much as the Smoot-Hawley-regulated trade.

It was passed, incidentally, as you and I both know, some 8 months after the stock market crash of October 29, 1929. It was not passed until June 1930, so it did not cause the crash.

Only 2½ years later, with Cordell Hull, we got reciprocal free trade, which started rebuilding America.

Reciprocal. Ah, they did not holler about just free trade; they said reciprocity.

Do you wish to comment or elaborate or correct me in any way, because you are my authority now.

Mr. REINSCH. Well, I am compelled, Mr. Chairman, to stand behind what I said then, and I said then and I will say again I think Smoot and Hawley got a bad rap as far as the Depression is concerned. I think there is no question about that.

I think it is also fair to point out that the enactment of that law did not do much to bring us out of the Depression.

It is probably fair to say that the Reciprocal Trade Act did not do much to bring us out of the Depression, either. What brought us out of the Depression was the war.

The more relevant point is that that was then, this is now. The world is a very different place now than it was then. The volume of trade at that point was much smaller. It is interesting to observe that, as I recall, the real difference in trade volumes was impacted more than anything else by World War I and the aftermath of World War I. The volume of world trade did not reach 1913 levels again in real terms until about the late 1980s or late 1990s. It took us that long to recover in terms of total volume.

Nevertheless, here we are and I think the important question, and you have raised it in your earlier remarks, is what kind of world are we in now and how do we deal with the changes that are occurring and which way do we go. In some respects we do not have as many choices as we used to. The economy is not as insular.

I will tell you a story, if I may. I used to talk about trade by saying more than 60 percent of the cut flowers sold in this country

every day are imported, which is true. It used to be 50; now it is 60. The important point about that fact is that 20, 30 years ago you could not do that, because we did not have a transportation structure that would allow that to occur. Now we do and people have taken advantage of it.

I gave that speech once to the Eastern North Carolina Chamber of Commerce. I am not quite sure where they are located, but it is sort of east of I-95 there somewhere. Some guy came up to me afterwards and said: "You know, that story, that is very interesting, but that is nothing; we have got a fish company off the coast of North Carolina that goes out and catches fresh flounder every day in the Atlantic and sells them in the Tokyo fish market daily."

Now, leave aside for the minute how they get it into the Tokyo fish market. I do not know. But the point is that 20 years ago you could not do that either, because we did not have a transportation infrastructure that allowed you to ship fresh fish over that period of time. Now we do. Companies are taking advantage of that. Sometimes the advantage they take is a productive thing for the United States, sometimes it is not. But that is the reality we live in.

I want to join with my colleagues—and I was remiss in commending you as one of the few people in the Congress that really wants to have a debate about this. I think it is important. We are not asking the right questions and you are asking the right questions. We may not all have the same answers, but you are to be commended.

The CHAIRMAN. That is the whole purpose. Really, we could not accomplish what is really needed in one hearing.

What we are trying to do is open it up. That is why we oppose Fast Track, because we need that debate to find out where we are and where we are headed.

I can tell you, though, we have got what you call the Sargasso Sea right within 50 miles of my home, and we have been shipping those eels to Japan for 30 years, because they like fish, they like eels, and they love flounder and everything else of that kind.

But I have also got West Virginia Pulp and Paper and they tried to sell cigarette paper, and they said: "Oh no, we smoke a different kind of cigarette with a different paper." So they spent $2 million and they got with the best of development labs in the paper industry, and they have got them right there in Charleston. So they developed a paper, you could not tell the difference between what the Japanese had and they had, and they still, after spending $2 million, they could not sell the paper.

They have always got these barriers. You are right, everybody raises these barriers around, and that is the description of the global economy. The global competition is controlled trade, it is not free.

The Secretary—I did not want to sound like an upstart, but he said we want to lead in world trade. What we are doing is leading in world trade deficits. What kind of leadership is this? We are going out of business.

Dr. Tonelson, we really need better data. I worked with Herman Stabman and now going through four Secretaries of Commerce, and

I know in the 1979 figure given us by the Department that 41 percent of what we consumed in America was imported. The majority now, I am convinced, is imported. There is not any question in my mind.

Yet I cannot get that figure. I have talked to Secretary Evans about it. He is going to try to start getting us better records. We need better data, because, like you say, they do not want to give the figures out about the jobs. They are not creating jobs at all. They are going, and you can understand it.

If you can save 10 percent of volume with respect to moving to an offshore low-wage country, if you have got $500 million in sales, it is actually a 20 percent saving. If you have got $500 million in sales, doctor—well, I think it was James Goldsmith who appeared before this Committee several years back, a very successful businessman. He says you can keep your executive office, your sales office in-country, but move your manufacturing offshore. $500 million in sales, you can make before taxes $100 million, or you can continue—and that is the job policy of the Congress—you can continue to work your own people and go out of business because your competition has gone. They are moving.

We are losing. The net loss, like I say, in my little State since NAFTA is 35,000 manufacturing jobs. We heard Senator Allen, actually he has had, since NAFTA, a 25 percent loss of manufacturing jobs in the State of Virginia.

So what we have got to do is get this debate and get it out into the open and realize the direction. Adlai Stevenson said: “It is not a question of whether I am conservative or I am liberal; am I headed in the right direction.”

The direction we are headed, Dr. Luttwak, you are right about the Brits. They told them after World War II: “Do not worry; instead of a nation of brawn, we are going to be a nation of brains; instead of producing products, we will provide services; instead of creating wealth, we will handle it and be a financial center.” And they have gone to hell in an economic handbasket over there.

They have got two levels of society. They have got nothing but the debating parliamentarians and scandal sheets, and that is the way we are headed. We have this big debate going on hollering “the economy is good, surpluses,” when there is not any surplus. I have got it in my pocket. I get it every morning. Let us see. We are now in the red this fiscal year, the year 2001, $59 billion. We ended up last year with $23.2 billion in the red, deficit.

We have had a deficit since Lyndon Johnson. I voted for the balanced budget then of $3.2 billion, and that was not because we went to the unified budget, or whatever, that used Social Security funds.

But we do not have surpluses and yet we talk about surpluses. The Secretary says the economy is good when it is going down into the pits, and not to be concerned about this trade deficit in excess of $400 billion is very, very bothersome, because we are going to run into a wall here before long. We will not be able to sustain as a world power.

I believe Morita was right in that sense, that you have got to be able to produce, develop a strong middle class. That is the strength of a democracy.

I have got a long list here, but we have got another thing coming up, and you folks have waited and been very patient. Let me keep the record open, if you do not mind, for questions.

Any further comments from any of the three? We would be delighted to have it. We will keep the record open for the other Senators, because I have been noticed they want to submit some questions to each of you. And we will have you back. Thank you very, very much for your appearance here today. The hearing will be in recess subject to the call of the chair.

[Whereupon, at 12:06 p.m., the hearing was adjourned.]

APPENDIX

PREPARED STATEMENT OF HON. ERNEST F. HOLLINGS, U.S. SENATOR FROM SOUTH CAROLINA

"A NORTH AMERICAN COMMON MARKET"

The foundation of American foreign policy has been our steadfast commitment to freedom and democracy. Yet, with the fall of the Berlin Wall when we should be doing everything in our power to foster and nurture the development of genuinely democratic governments around the world, supporters of the North American Free Trade Agreement (NAFTA) would head us in the opposite direction. They ignore our historic commitment to freedom and human rights by entering into a "free trade agreement" whose principal beneficiary will be Mexico's ruling oligarchy. For the past 60 years, that oligarchy has systematically denied its citizens free elections, free speech, basic civil liberties and a genuinely free market.

Instead of pursuing this narrow economic agreement inherited from the previous Administration, President Clinton should enunciate a broad vision for the Americas that encompasses not just economics and trade, but also political and social reform. As former Secretary of State George Shultz said, "The embrace of free market economics is not sufficient to justify political repression." Now, as never before, the benefits of a truly free market will be enjoyed only when the market is buttressed by strong democratic institutions.

Previous American initiatives to boost democracy in Latin America fell short of their lofty goals. President Franklin Roosevelt's Good Neighbor policy, President John F. Kennedy's Alliance for Progress and President Ronald Reagan's Caribbean Basin Initiative failed because our commitment to democratic and social reform never matched our rhetoric. Billions of dollars in aid money were squandered by corrupt regimes who were more interested in helping themselves than with raising living standards. For example, we propped up the Shah of Iran for decades, only to reap the whirlwind of militant Shiite fundamentalism. We embraced the Somoza oligarchy in Nicaragua and wound up with the evangelical Marxism of the Ortega brothers.

Today, the country at issue is Mexico. We have an historic opportunity to foster democratic institutions and genuine economic development on our southern border. Our choice is clear: We can be a force for change to promote democracy and build a thriving middle class. Or we can align ourselves with the ruling oligarchy that thwarts the Mexican people's aspirations for representative democracy.

In more than 2,000 pages of the NAFTA text, the word "democracy" does not appear. NAFTA only locks in the status quo in Mexico. I propose an alternative approach that puts democracy first and rewards democratic progress with economic and trade privileges culminating the creation of a North American Common Market—a partnership whose membership is predicated upon a shared commitment to the basic principles of a democratic society: free elections, free speech and free markets.

THE ILLUSION OF REFORM

Throughout Mexico's history, a number of Mexican leaders have promised to wipe out corruption and reform the political system. Even Porfirio Diaz, Mexico's turn-of-the-century dictator, arranged electoral charades to create the illusion of democracy. While current President Carlos Salinas de Gortari has instituted substantial reforms, he has been careful not to challenge the power structure that has ruled Mexico for the past 60 years.

Today, U.S. editorial writers hail Salinas and his American-educated technocrats as valiant reformers who have cleaned up a corrupt political system and overhauled an inefficient statist economic system. In truth, however, the "new" Mexico is strikingly like the old. Most of the political reforms undertaken by the Salinas Administration are nothing more than window dressing designed to mollify NAFTA's critics in the United States. As the Salinas era ends, a careful examination of the record

shows that for all the international fanfare, the actual political reforms have been modest and largely cosmetic. Human rights violations, electoral fraud and corruption remain endemic in Mexico. Writing in the September/October edition of *Foreign Affairs*, professor Jorge G. Castañeda said: Mexico's underlying problems persist. It retains a largely corrupt and unchallenged State that possesses only the merest trappings of the rule of law. The enduring obstacles to Mexico's modernization—its repeated failure to transfer power democratically or to remedy the ancestral injustice of its society—remain and will require Mexico to continue to change itself, with or without a trade accord.

Even *The Economist* acknowledges, "The ugly truth is that Mr. Salinas and his band of bright technocrats, adored though they are by the great and good of the international conference circuit, wielded power courtesy of PRI fixers and worse in the countryside." While former U.S. Presidents and Secretaries of State sign their names to op-ed pieces praising Mexico's reforms, the State Department's February 1993 report on human rights paints a starkly different picture. It details the Mexican government's complicity in electoral fraud, torture, politically motivated murders, suppression of independent labor unions and systematic control of the media.

"To maintain power the PRI [Institutional Revolutionary Party] has relied on extensive public patronage, the use of government and party organizational resources, and according to respected independent observers, electoral fraud," the State Department report said.

Mexico's "reforms" are nothing new. Our neighbor has a long history of either passing progressive legislation governing labor and human rights, or of signing international agreements that ostensibly guarantee these rights. Mexico also has a long history of not living up to these agreements.

In 1990 with great fanfare, President Salinas presented a new Federal Election Code and established a Federal Electoral Institute. These electoral reforms might appear a dramatic departure from the past. But in reality, they are only designed to legitimize the status quo while giving the illusion of fairness. It is important to note that the new Electoral Commission is not independent. Instead, it is stacked with members of the ruling party. In addition, the final arbiter of elections is the Minister of the Interior—the Mexican official charged with maintaining domestic order. That position is currently held by Patrocinio Gonzalez, former Governor of the State of Chiapas. It is widely recognized that his term as Governor was marked by widespread electoral fraud and the imprisonment of Indians, teachers and Catholic priests who dared to challenge the ruling party.

Despite the enactment of electoral reforms, Mexican elections continue to be exercises in deceit. As recently as 1992, gubernatorial elections in Michocán were marked by widespread fraud and the PRI candidate was forced to step down, only to be replaced by another hand-picked candidate.

This winter, the atmosphere of fraud will continue. Like the PRI's rulers before him, President Salinas will engage in the Byzantine ritual of tapping his successor—a process appropriate for Yale secret society, not a representative democracy. The state then will throw its tremendous financial and media resources behind the anointed successor, who, in all likelihood, will be the figurehead for Mexico's elite 300 for another 6 years.

HUMAN RIGHTS RECORD

More than a decade ago, then-Deputy Secretary of State Warren Christopher, highlighted the importance of the link between human rights and the free market. "Respect for human rights creates an atmosphere for stability in which business and investment can flourish." Yet Mexico's record on human rights is not consistent with the Clinton administration's emphasis on basic human dignity.

The State Department's human rights report notes, "Several politicians and human rights activists were killed in 1992," and that "[t]here continues to be cases of extrajudicial killing by police." Although Mexico has established an independent commission on human rights, the State Department notes that "its recommendations have been implemented only partially."

According to the State report, other human rights abuses committed by the Mexican government include torture—"the most commonly used methods include threats, beatings, asphyxiation, and electric shock"—and "frequent incidents of arbitrary arrest and imprisonment." In 1992, the United Nations Committee Against Torture strongly criticized Mexico's record of "torture with impunity."

MEDIA CONTROL

Threats, intimidation, and violence are not the only means that Mexico's ruling party uses to maintain its hold on the reins of power. In an era in which the rapid

dissemination of information helped bring down the Berlin Wall, Mexico's ruling party tightly controls access to the public media.

Until last month, one of Mexico's two principle television stations was owned by the government. The other network was safely controlled by one of the PRI's top fund-raisers, Emilio Azcarrega. Recently, the Mexican government announced that it was selling the government-owned station to yet another PRI fund-raiser—Ricardo Salinas Pliego—who will continue the station's pro-government and pro-party slant.

In fact, after gaining control of the station, Salinas Pliago frankly stated that he will have to continue its pro-government programming because "Mexico is not yet ready for democracy."

Although Mexico has independent newspapers and magazines which give the illusion of a free press, the State Department human rights report shows that there are "significant restrictions on press freedoms."

A PERFECT DICTATORSHIP

Perhaps Peruvian writer Mario Vargas Llosa offered the best description of the Mexican political system. In describing Mexico as the "perfect dictatorship," Llosa wrote that it is "the permanence of a party not a man, a party that is unmovable, a party that gives enough space to criticism, as long as it serves its interests, because in this way it shows that it is a democratic party; but suppresses by any means the criticism that somehow endangers its permanence."

A fundamental question that has never been addressed is whether Mexico's tradition of authoritarian, one-party rule is compatible with our form of democratic capitalism. Senate Finance Committee Chairman Daniel Patrick Moynihan has succinctly framed the debate on NAFTA: "How can you have a free trade agreement with a country that hasn't had a free election?"

NAFTA proponents argue that NAFTA will raise living standards and gradually harmonize upwards wages and working conditions. Commentators are quick to praise the dramatic economic reforms that have transformed the Mexican economy. A recent editorial in *Financial World* proclaims, "Over the past several years Salinas has moved with great domestic risk toward opening what once was one of the most protected, corrupt and government-controlled economies. Should NAFTA fail—or die a slow death as the U.S. equivocates—Salinas's efforts would be discredited and the old order could return." The obvious flaw in this argument is that the old order has not been swept away. As in the case of the political reform, the tight-knit group that for decades has exercised political and economic power has not been challenged.

AN ELITE IN CONTROL

Augustin Legoretta, a prominent businessman and former president of BANAMEX (one of the principal banks in Mexico), provided this candid assessment of how the Mexican economy operates: "A very comfortable little group of 300 people make all the economically important decisions in Mexico." This comfortable group has acquiesced in the government's decision to tear down the "Gringo Go Home" sign and open their country to foreign investment by offering a low-wage, high-productivity platform for export into the United States. In return for supporting Salinas's economic reforms, Mexico's corporate elite have enjoyed a financial bonanza. Mexico's high-flying stock market, the "Bolsa Mexicana," has created paper millionaires and even billionaires. Before Salinas took office, *Fortune* listed two Mexicans in their list of billionaires; 6 years later there are twenty-two. Not surprisingly, the Salinas administration's ambitious privatization policy has rewarded many of the President's closest political associates: Carlos Slim, a financier and PRI fund raiser who won control of the telephone company TELMEX one of the state run banks; Pablo Brener, another PRI fund raiser who was awarded Mexicana Airlines; and Jorge Larrea, a close friend who now owns CANNEA, the country's largest government-owned copper mine.

Questions have arisen over the conduct of Mexico's privatization programs, including whether there is a truly competitive system of open bidding. In addition, U.S. companies are allowed to own only minority interests in these companies. Under NAFTA, Mexican negotiators have been careful to protect the powerful interests that have benefited from the privatization. For example, the Mexican conglomerate VITRO, a world class maker of flat glass, will benefit from a 10-year phase-out of the tariff on flat glass while the U.S. tariff is phased out immediately. Similarly, the recently privatized banking system will benefit from 10 years of protection, and U.S. banks will be strictly limited to a small percentage of the Mexican market. To reward the PRI for their "business-friendly environment," Mexico's top financiers

held an intimate—and expensive—dinner party, with guests pledging $25 million each to the ruling party. One participant even boldly proclaimed that he would be willing to pledge twice this amount because he had prospered so handsomely during the Salinas Administration. While the proponents of NAFTA praise the "free market" reforms in Mexico, in reality, Mexico is pursuing a development model that leaves very little to the magic of the marketplace.

A CLOSED ECONOMIC SYSTEM

Far from being a model of free market development, Mexico is following a much different path, as Finance Minister Pedro Aspe Armella described in 1991: The postwar experience [has called into question] the assumption underlying . . . comparative advantages [that] were more persuasive in the eighteenth and nineteenth centuries when many industries were fragmented, production was more labor- and less skill-intensive, and much trade reflected differences in growing conditions, natural resources and capital . . . Widely applicable technologies such as microelectronics, advanced materials and information systems have rendered obsolete the traditional distinction between high and low technology industries.

BusinessWeek went further in a cover story: In their drive to modernize Mexico, Salinas and his planners command nearly every variable of the economy. To smother inflation and preserve Mexico's huge labor cost gap with the U.S. and other producers, Salinas fixes salaries through a complex business labor agreement known as *el pacto*. He anoints and boots out labor union bosses and State Governors alike. A few years ago, he quietly banished an obstreperous American president of Chrysler de Mexico, who was quickly replaced by a Mexican. Salinas and his technocrats juggle import duties and steer investment from one region to another. In short, Salinas and his number crunchers run a near command economy much closer to the Asian model than any country in the West.

Mexico has received international accolades for producing an economic miracle, yet growth has averaged only 2 percent for the past 6 years. During the dark days of import substitution, Mexico's GDP grew by over 4 percent. However, much of this "growth" was the result of flight capital that has returned to earn higher interest rates.

For the "elite 300" who have reaped huge rewards from privatization, Mexico's reforms have produced unprecedented wealth; unfortunately, much of this wealth has been achieved at the expense of the Mexican worker. The World Bank, noted that Mexico's 1992 per capita GDP was 5 percent below the country's 1980 per capita GDP. In the last 10 years, on average, Mexicans have seen their take-home pay decline by 40 percent. In a country that already suffers from one of the worst income distributions in the Western Hemisphere, Mexico's "new" development path has exacerbated the gap between rich and poor. Over the last decade, the richest 10 percent of the population saw its share of the national wealth increase by 15 percent. During the same period, 25 percent of Mexico's tiny middle class fell into the ranks of the poor. In addition, half of the country still does not have electricity or running water; some Mexican states advertise labor for 99-cents-an-hour; and 12-year-olds are included in the official labor statistics.

JOBS AND CONSUMER GOODS

To provide foreign investors with a pliant work force, the government has actively intervened to thwart the formation of independent trade unions. When a renegade labor leader tried to organize the Maquiladora plants, the Mexican government promptly arrested him. When workers at Volkswagen tried to form an independent union, President Salinas personally intervened, using the Mexican army to force a violent end to the strike. He later acquiesced in Volkswagen's decision to fire all 14,000 workers and rehire only those workers who pledged not to join an independent union. Smashing independent unions and freezing wages at third-world levels is not consistent with the stated goals of the "aperatura," or "economic opening," which in theory raises living standards. As *BusinessWeek* noted, the irony of the Salinas era is that "many Mexican workers still can't afford to buy the products that they turn out."

Advocates of NAFTA believe the agreement will not spur the flight of jobs south of the border. They argue that the trade liberalization envisioned in NAFTA will increase U.S. exports to Mexico, and therefore increase jobs in the United States. To support this claim, they point to our burgeoning trade surplus with Mexico. Since Mexico opened its economy to U.S. exports, our former trade deficit has been replaced by a $4 billion surplus. Under Salinas, Mexico's trade picture has significantly deteriorated. This year, Mexico's overall trade deficit will balloon to $20 bil-

lion. Consumer demand, however, accounts for only a small portion of our trade with Mexico. According to the trade statistics provided by Mexican trade officials to U.S. negotiators, 55 percent of U.S. exports never enter the Mexican market. They are simply parts shipped to gleaming U.S.-owned factories for assembly and re-shipment back to the United States. This is how the Brookings Institute's Nora Lustig explains Mexico's current account deficit:

"The good news [for Mexico] is that the highest increase is to be found in capital goods imports (24.8 percent) and the lowest in consumer goods (10.6 percent) This upsurge in imports is in part a response to the expansion of productive capacity in anticipation of Mexico's positive outlook.

"The current large imbalance in the trade account may well be a one time phenomenon in the sense that it is the result of modernization of the productive plant that will soon render its fruits in the form of higher net exports. If the current expansion pays off in higher productivity growth in the future, the disequilibrium will disappear and so will the real appreciation of the exchange rate."

Our own trade data support this position. The majority of U.S. exports are in two categories: capital goods and industrial supplies. U.S. Trade Representative Mickey Kantor points with pride to the fact that the fastest growing segment of U.S. exports is in consumer goods. A close examination shows that they are growing from a small base and still account for a smaller overall percentage of our exports. With a per capita income of approximately $3,000—still 5 percent below Mexico's 1980 level—and one of the worst income distributions in the Western Hemisphere, Mexico will take years—if not decades—to become a significant market for consumer goods.

IT'S THE LOCATION, STUPID

That much-ballyhooed "great sucking sound" of American jobs going to Mexico because of NAFTA will be heard loud and clear in another incarnation. NAFTA will suck foreign companies into Mexico so they can win cheap, duty-free entry into the U.S. market. For years, Asian investors, particularly Japanese burned by Mexico's debt crisis, have been reluctant to invest in Mexico without adequate protection for their investment. NAFTA will provide that protection, which is why *Niki Weekly* notes that the "Bank of Tokyo is Bullish" on NAFTA. And that's why Volkswagen executives boast they will use Mexico as their launching pad into the U.S. market. But European and Japanese companies are not alone. The Korean government is providing tax incentives for companies that open in Mexico. China's Communist government-owned textile company is opening a yarn-spinning operation in Mexico.

SOWING THE SEEDS OF DISCONTENT

If we rush to pass a NAFTA which sanctions a program of economic development based on the suppression of wages and living standards, we will be sowing seeds of discontent among the Mexican masses. Rather than building a stable economic partner, we will create the conditions for civil unrest. Indeed, the classic prescription for civil unrest is an entrenched, aloof leadership that raises the expectations of its populace. When the expectations are not met, civil order breaks down.

As the PRI pursues a policy that beats down wages while demanding increases in productivity, the basic needs of the work force will go unmet. Without democratic institutions to serve as a check against arbitrary power, Mexico will remain a haven for the exploitation of labor and the environment.

NAFTA supporters argue that our two economies are already in the process of integration. This is true, which is why we have an unprecedented opportunity to encourage Mexico to adopt genuine political and economic reforms. But the proponents of NAFTA have never advocated using this process as a way to encourage fundamental change in Mexican society. Instead, what NAFTA advocates propose is a historical first—a shotgun marriage between a developed, First World Nation and an undeveloped, Third World country. As hundreds of thousands of unemployed American workers have discovered, "The jobs in the U.S. that are vulnerable are not the $6-an-hour jobs, but the $18-an-hour ones. It goes to the core of the U.S. industrial base," labor economist Harley Shaiken told *BusinessWeek* in 1992.

Furthermore, the Administration and some Members of Congress believe that tacking on hastily arranged side agreements regarding labor and the environment will correct an approach to hemispheric integration that locks in Mexico's status as a low-wage export platform. But ill-conceived side agreements cannot rectify a pact based on a flawed premise. No side agreement can adequately redress the tremendous disparity between our economies. Nor will side agreements improve enforcement of labor laws or environmental regulation.

Mexico has adopted tough laws to protect labor and the environment, but its commitment to enforcement is inadequate. While the Mexican constitution provides im-

pressive guarantees for the formation of independent labor unions, it is widely known that the PRI controls labor bosses. In addition, a 1992 General Accounting Office survey found that none of the American-owned plants they surveyed in Mexico complied with Mexico's environmental regulations. Also, several media organizations have documented the environmental disaster festering on the border.

Finally, while NAFTA does not address immigration, the treaty's proponents proclaim that it will slow the tidal wave of immigrants across the border. They argue that as new factories open in Mexico and more jobs are created, immigration will slow because workers will choose to stay home. This, however, is not borne out by recent history or demographics. The explosion of Maquiladora plants along the Mexican border has only served as a training ground and springboard for Mexicans eager to flee squalor. Maquiladoras have suffered tremendous turnover—the average worker stays 18 months before he seeks higher wages in the U.S. Finally, Mexico's economy will have to grow more than 6 percent a year to accommodate the 1 million new workers that enter the workforce each year and the hundreds of thousands of agricultural workers that will be displaced by the opening of Mexico's agricultural market. And since few predict that the Mexican economy will grow by 6 percent, Mexico's surplus workers likely will head north.

CREATION OF A NORTH AMERICAN COMMON MARKET

Instead of rushing pell-mell to integrate an underdeveloped economy with a developed economy, we should follow the example set by the European Community. The Community's decision to integrate Spain, Portugal and Greece was the result of several years of intense negotiations. As a pre-condition of accession to the Community, the Council of Europe required these nations to adopt significant reforms to their political and economic systems. Indeed, the preamble of the accession agreement states, "The principles of pluralist democracy and respect for human rights form part of the common heritage of the peoples of the states brought together in the European Communities and constitute essential elements of membership."

Furthermore, for several years Turkey has unsuccessfully sought admittance to the Community. According to the Director General of the Community, Turkey is not an appropriate candidate for membership for three reasons:

1. Turkey's economy was not compatible with the EC's. Integration would result in huge costs to fit Turkey into the social framework of the Community.
2. The EC could not absorb Turkey's rapidly increasing population and unemployment rate.
3. Democracy in Turkey still lacked extensive protection of individual civil and political rights.

The integration of Spain and Portugal involved a significant transfer of resources from the developed to the less developed regions of the Community. Spain and Portugal received over $5.4 billion per year from the European Regional Development Fund and the European Social Funds. These funds were used to assist both regions and individuals who might be harmed by each successive stage of trade liberalization. The proceeds of the funds were also used to stimulate investment and in the development of infrastructure in these countries. This is a policy we should adopt toward Mexico.

A North American Common Market would require the nations of North America to enter into a social compact to establish minimum standards for labor rights and environmental protection as well as a common commitment to protect the individual liberties that are the foundation of a democracy. A North American Common Market, with a common external tariff, could be an effective vehicle for competing with the emerging trade blocs in Europe and Asia.

Before admitting Mexico and other nations of Central and Latin America, the gross disparity in income levels must be addressed. To narrow the development gap, a fund similar to the European Regional Development Fund and the European Social Fund should be established to ease this transition. The proceeds of the fund would be devoted to upgrading Mexico's antiquated infrastructure and to cleaning up the environmental mess along the border.

Other developmental projects could be financed by swapping existing Mexican debt for development bonds backed by zero coupon bonds (U.S. Treasury notes). In addition, the U.S. should expand debt relief proposals. Latin America's crushing debt burden is still a significant impediment to its sustainable and equitable growth. Previous attempts at debt relief failed to make a significant dent in Mexico's outstanding debt. Even after implementation of the Brady Plan, approximately 30 percent of Mexico's export revenues are devoted to debt service; if both internal and external debt are counted, the figure jumps to 45 percent. Thus, revenue generated

by Mexico's outward-looking economic policy is flowing out of the country rather than being used to raise living standards throughout Mexico.

The integration of countries with such disparate levels of development will also require close coordination of macroeconomic and investment policies. Finance ministers should establish investment guidelines to prevent the wholesale de-industrialization of the developed areas of the North American Common Market. In addition, exchange rate policy should be coordinated to prevent competitive devaluations that would depress wages and destabilize current accounts.

Finally, entry into the Common Market must be predicated on the adoption of real democratic reforms that produce free and fair elections. Only after Mexico becomes a functioning democracy will the gap in income levels and wage rates narrow. Once this is accomplished, Mexico, the U.S., and Canada should proceed with wholesale elimination of tariff and non-tariff barriers.

CONCLUSION

Thirty years ago, another young vigorous President offered the Americas a vision of shared destiny, but one that addressed both economic change and social/political change. As John F. Kennedy said, "No program that is restricted to the technicalities of economic development can fully answer the needs of the Americas. Only an approach to economic progress and social justice which is based on the wide acceptance of the fundamental ideals of political democracy and human dignity can conquer the many ills of our hemisphere and respond fully to the aspirations of our people."

After decades of ignoring the calls for change, it's time we align ourselves with the forces of change and renew our common commitment to economic and social progress. If we don't promote real democratic change in Latin America and champion economic growth at home, the United States could fulfill Harvard economist Richard Freeman's fear: "One possibility is for us to become a class society like those in Latin America . . . That's the direction we're headed."

○